Arizona Public Service Company
P.O. BOX 53999 • PHOENIX, ARIZONA 85072-3999

September 12, 1996

Docket Control
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

Re: Docket No. U-0000-94-165

Dear Sir or Madam:

Pursuant to Arizona Corporation Commission letter dated August 28, 1996, Arizona Public Service with other interested parties was invited to submit comments on the proposed rule to introduce retail competition in Arizona.

Attached is an original and ten copies of Arizona Public Service Company's comments. If you have any questions, please contact me at 250-2031.

Sincerely,

Barbara A. Klemstine
Manager
Regulatory Affairs

BAK/JKD/pb

Attachment

CERTIFICATE OF SERVICE

The original and ten (10) copies of the foregoing document were filed with the Arizona Corporation Commission on this 12th day of September, 1996, and service was completed by mailing, hand-delivering or faxing a copy of the foregoing document this 12th day of September, 1996 to all parties of record herein.

Barbara A. Klemstine

COMMENTS ON

ARIZONA CORPORATION COMMISSION

STAFF'S DRAFT RULES

OF

AUGUST 28, 1996

DOCKET NO. U-0000-94-165

ARIZONA PUBLIC SERVICE COMPANY

SEPTEMBER 12, 1996

COMMENTS OF ARIZONA PUBLIC SERVICE COMPANY ON COMMISSION STAFF'S DRAFT RULES

Arizona Public Service Company ("APS" or "Company") hereby submits its comments on the draft rules on retail electric competition ("Draft Rule(s)") circulated by the Utilities Division Staff ("Staff") of the Arizona Corporation Commission ("Commission") on August 28, 1996.

APS is and has been an active proponent of increased competition. However, the Company cannot and does not agree with the process by which the Draft Rules were created or many of its substantive provisions. The Commission must first carefully consider, through open evidentiary hearings that can begin as soon as the Commission is ready, and then decide such fundamental issues as customer impact, reliability, compensation and utility service obligations before, and not after, the Commission attempts to drastically restructure the State's multi-billion dollar electric industry. The Draft Rules has the process totally reversed in clear violation of the law and sound public policy.

In this response, APS requests Staff to set aside the Draft Rules, which APS believes are clearly unlawful, and instead work with affected parties and the Commissioners to develop certain fundamental principles that would govern future steps in restructuring. The already scheduled September 18 workshop would provide an opportunity to discuss and debate those principles. Such principles could thereafter be adopted by the Commission. Such a far more rational process should not delay the introduction of effective and efficient competition that will benefit the State without compromising its legal obligations to the regulated utilities that have served its customers well.

In this response, APS also provides specific comments on the Draft Rules. The Draft Rules pose threshold legal issues repeatedly raised by the Company and others but left unaddressed by Staff in development of its Draft Rules. Therefore, APS' comments begin with a legal analysis addressing the Commission's fundamental lack of authority to unilaterally introduce direct retail electric competition, as well as other substantive and procedural legal concerns. APS also presents a section-by-section analysis of the Draft Rules, with suggestions and alternatives where appropriate.

APS requests the Staff to: (1) carefully review these comments and the comments submitted by other parties in this Docket; (2) "table" the Draft Rules, and (3) establish a procedural schedule whereby parties whose interests are affected by the Draft Rule can participate with the Commission and the Legislature in the development of a legally sound, practical and efficient process to achieve retail access in an equitable manner and as soon as issues of reliability, compensation, reciprocity, etc., have been resolved.

I. SUMMARY

Based upon a review of existing law in Arizona, APS believes that adoption of the Draft Rules would not be a lawful action by the Commission, both substantively and procedurally. The Commission does not possess the authority to require retail electric competition between public service corporations ("PSCs"); nor does it have the authority to regulate municipal and other non-PSC utilities. Similarly, the Commission lacks the power to: set rates for transmission and related ancillary services which power resides exclusively with the Federal Energy Regulatory Commission (the "FERC"); authorize violations of territorial agreements previously approved by the Commission; create a discriminatory

regulatory scheme favoring newly certificated competitors over incumbents; or dictate specific investment decisions by public service company management contrary to existing regulatory requirements.

The Draft Rules are legally deficient in their treatment of just and adequate compensation required for the transition to a competitive marketplace, including stranded costs. They fail to provide just and adequate compensation for the unconstitutional "taking" of utility property and the impairment of APS' contract with the state. Additionally, the Draft Rules violate certain provisions of APS' Rate Reduction Agreement approved by the Commission this past April.

Finally, APS submits that the Draft Rules do not provide for the fundamental statutory and due process rights of APS and other "Affected Utilities" because they purport to modify and in some cases even rescind their existing certificates of convenience and necessity ("CC&N") without proper notice and an evidentiary hearing; or without the requisite finding that APS or the other "Affected Utilities" are unable or unwilling to provide electric service in their respective certificated service areas at a reasonable rate.

In addition to these legal issues, APS has also prepared specific comments to many of the sections of the Draft Rules. These comments range from concerns on principles that we believe were not sufficiently addressed to specific wording changes, and include a proposed alternative to the solar portfolio standard.

Preliminary Considerations

As indicated previously, APS favors the introduction of retail electric competition in Arizona. Since 1988, the Company has been engaged in aggressive cost management measures with one goal in mind: favorably positioning APS for effective participation in a more competitive utility market in Arizona. These measures have already yielded significant, noteworthy benefits to APS' consumers, including materially lower operating costs, stabilized rates and continuing rate reductions, innovative consumer programs and aggressive resource management. The Company has publicly pledged its commitment to a process by which its consumers will realize the benefits of lower cost electricity at consistently high levels of reliability. For this reason, APS has proposed a comprehensive, lawful and workable plan -- the Arizona Customer Choice Plan -- that will introduce effective retail access to Arizona consumers as soon as fundamental legal, regulatory, technology, logistical and compensation issues have been resolved.

The FERC and other states have set in motion a process which can provide lower cost electricity to consumers at the retail level – and which cannot be ignored by the Commission and electric utilities in Arizona. However, no matter how beneficial the outcome promises to be, it cannot be attained without careful consideration of important principles which substantially impair the benefits to be obtained. The quest for favorable economics cannot alone be the end that justifies the means. Arizona's electric utility industry represents a stable, reliable and efficient resource upon which the state's economic health and public safety depends. Any process that seeks to adjust the way in which that resource functions must first be dedicated to assuring that the electric system continues to function in a reliable manner.

Recent events in Arizona and the Western Region of the United States as a whole have raised reliability concerns to a higher level. Although not a result of competition, the recent power outages experienced

throughout the western United States serve as a reminder of our dependence on electricity and the importance of maintaining reliability in the delivery of electric service to customers. Any program that injects competition into electric retail service without considering this threatens to undermine the ability to continue reliable service at a level upon which Arizonans depend.

To date, APS has repeatedly expressed concern that the process thus far has not produced a proper factual basis upon which the Commission can rationally proceed. The Draft Rules represent the continuation of that flawed process, which are both contrary to the state's public policy and prevailing Arizona law. Although APS supports the introduction of retail electric competition in Arizona, the transition to a competitive marketplace must be undertaken in a way that respects basic, long-standing public policy and legal considerations and the operating reliability and efficiency of the electric system in Arizona.

Specifically, the ACC must deal with the fact that the law in Arizona deprives it of the power to order utilities to open their service areas to competition. The rules contained in the draft proposal which directly or indirectly have the effect of requiring electric utilities to open up their exclusive service areas to competition -- namely R14-2-xxx2, R14-2-xxx3, R14-2-xxx4, R14-2-xxx5, R14-2-xxx8, R14-2-xxx12, and R14-2-xxx15 – are contrary to long-standing legal principles in Arizona that underwrite achievement of the state's public policy that electric utilities operate as regulated monopolies.

As the regulatory authority charged with overseeing the provision of reliable, reasonably priced electric service in Arizona, there is no arguing that the ACC has an important role and leadership position in this process. But the citizens of Arizona have not given the Commission the legal authority to unilaterally impose retail electric competition.

II. LEGAL CONSIDERATIONS

The Draft Rule serves to entirely reshape an essential industry in Arizona. Although Staff suggests that a number of opportunities were made available for input on electric industry restructuring (although not on the Draft Rules), the breadth and content of the Draft Rule has been developed by Staff without the benefit of an open discussion by the utilities, Commissioners or other parties on these important issues. If it is the intent of the Staff to provide this opportunity in the future, it would be helpful to understand the timing, format and decision process the Commission intends to take. In particular, this includes the legal concerns that go to the Commission's authority to implement retail electric competition in Arizona as well as the practical realities that have been expressed thus far in the proceeding by many participants, including APS. Similarly, APS is not aware of any opportunity for the Commissioners to participate in shaping this abrupt change in over 80 years of regulation. In this respect, then, the Draft Rule as it stands today is not the result of reasoned, substantial evidence.

a) THE COMMISSION HAS NO AUTHORITY TO REQUIRE OR AUTHORIZE RETAIL COMPETITION BETWEEN ELECTRIC UTILITIES

It is beyond question that the historic and existing regulatory scheme in Arizona as to electric utilities is one of regulated monopoly. In *James P. Paul Water Company v. Arizona Corporation Commission*, 137 Ariz. 426, 671 P.2d 404 (1983) the Arizona Supreme Court expressly stated:

> Once granted, *the certificate confers upon its holder an exclusive right to provide the relevant service* for as long as the grantee can provide adequate service at a reasonable rate. If a certificate of convenience and necessity within our system of regulated monopoly means anything, it means that its holder has the right to an opportunity to adequately provide the service it was certificated to provide. *Only* upon a showing that a certificate holder, presented with a demand for service which is reasonable in light of projected need, has failed to supply such service at a reasonable cost to consumers, can the Commission alter its certificate. *Only* then would it be in the public interest to do so. A system which did not provide certificate holders with an opportunity to provide adequate service at reasonable rates before deletion of a certificated area would be *antithetical to the public interest* for several reasons. *First, it would encourage price competition between public service corporations, the very mode of operation which the Legislature has rejected.* [Emphasis supplied.]

Id. at 429; *see, also, Metro Mobile CTS, Inc. v. Newvector Communications, Inc.*, 661 F. Supp 1504, 1509 (D. Ariz. 1987) ("The Arizona constitutional and statutory scheme clearly and affirmatively sets forth a policy to displace competition with regulation as to public service corporations."). The holding of *James P. Paul* was recently reiterated in *Tonto Creek Estates v. Arizona Corporation Commission*, 177 Ariz. 49, 58, 864 P.2d 1081 Ariz. App. (1993): "A certificate of convenience and necessity obligates the holder to serve an area *and is a grant of monopoly rights by the state*." [Emphasis supplied].

The public policy against competition and in support of monopoly service rights also extends to non-PSC electric utilities. *City of Mesa v. Salt River Project*, 92 Ariz. 91, 373 P.2d 722 (1962). Moreover, even before the *James P. Paul* decision was issued, regulated monopoly had been recognized by the Federal Courts as the clear and unmistakable public policy of Arizona. *Community Builders, Inc. v. City of Phoenix*, 652 F.2d 823 (9th Cir. 1981); *Metro Mobile, supra.*

Although *James P. Paul* was, in some respects, merely a particularly strong restatement of the traditional position on certificate rights enunciated by the Court in *Corporation Commission v. People's Freight Line*, 41 Ariz. 148, 16 P.2d 420 (1932) and *Application of Trico Electric Cooperative, Inc.*, 92 Ariz. 373, 377 P.2d 309 (1962), it has special significance for several reasons. First, the Court of Appeals had already reversed the Commission in *James P. Paul*, but the Arizona Supreme Court agreed to hear the case anyway because it felt the Court of Appeals' opinion was too soft on upholding incumbent certificate holders' rights. Second, both parties to the underlying territorial dispute in *James P. Paul* had been acquired by the City of Scottsdale prior to issuance of the Supreme Court's opinion. Yet, a request that the appeal be dismissed as moot went unheeded by the Court, which apparently believed that making a clear statement of the law was of paramount public interest. Finally, the issuance of the Court's opinion prompted a change in the law, as will be discussed in more detail later in this section of the Company's Comments.

The Draft Rules either ignore these unambiguous holdings of both state and federal courts or incorrectly assume that the Commission can simply change this public policy by enacting regulations. However, there are numerous Arizona decisions (including *James P. Paul*) clearly stating that the doctrine of regulated monopoly (and its implementation through exclusive CC&N's) is a *legislatively* created policy over which the Commission exercises no control or veto power:

> The concept of the regulated monopoly arose from the *Legislature* in granting the Commission the authority to issue certificates of convenience and necessity to public service corporations . . .
>
> That it is the *legislative* creation of certificates of convenience and necessity that gave rise to the concept of "regulated monopoly" was made abundantly clear by *Corporation Commission v. People's Freight Lines, Inc., supra.* [*Mountain States Telephone & Telegraph Company v. Arizona Corporation Commission*, 132 Ariz. 109, 114, 644 P.2d 263 (App. 1982).]
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> * * *
>
> Issuing certificates of convenience and necessity is far from a plenary power of the Commission. It is a *legislative power* delegated to the Commission subject to restrictions as the *Legislature* deems appropriate. (Emphasis supplied)

[*Tonto Creek Estates v. Arizona Corporation Commission, supra*, at 56.]

The Commission itself has clearly acknowledged the Legislature's preeminent and exclusive authority in this area. After the issuance of the *James P. Paul* decision in October of 1983 (and in light of a Superior Court reversal of a Commission order authorizing competition in the radio paging industry), the Commission proposed legislation in the 1984 session of the Arizona Legislature that would have amended A.R.S. § 40-281, *et seq.*, to remove the monopoly rights granted by a CC&N to *all* public service corporations. The Legislature would not accept such a general and fundamental change to its policy of regulated monopoly, but instead agreed to modify service area rights *solely* for telecommunications companies. *See* A.R.S. § 40-281(D). It was pursuant to that limited statutory change that subsequent competitive CC&Ns have been granted by the Commission in the telecommunications industry.

Indeed, it can be argued that the Draft Rule runs counter to the Commission's own accountability to the utilities over which it exercises jurisdiction:

> We hold that the Corporation Commission was under a duty to Trico to protect it in the exclusive right to serve electricity in the region where it rendered service, under its certificate.

Trico, 377 P.2d 373, 387. To the extent the Draft Rule is motivated exclusively by a quest for lower cost, it also violates the Commission's obligation to respect the expectation of the utilities it regulates. *James P. Paul,* 671 P.2d 426, 431.

Moreover, the Draft Rule does not consider the parallel efforts currently underway by the Arizona Legislature. Earlier this year, the Legislature formed a Joint Study Committee On Electric Industry Competition (*See,* House Bill 2504, Chapter 276). This Study Committee is comprised of broad representation, including members of the Arizona House and Senate, the Chairman of the Arizona Corporation Commission, the Director of the Residential Utility Consumer Office, consumer representatives, representatives of the economic development community, a representative of the Governor's Office, industry associations, utility representatives and representatives of low income consumers among others.

The Study Committee's responsibility is to evaluate how best to achieve a competitive electric market in Arizona so that the public interest is served, consistent with the perspectives of all affected parties. This Committee is to issue its final report by the end of 1997 for "implementation of the electric utility competition proposal, as approved by the legislature, to begin no later than December 31, 1999."

The Legislature recognized the issues related to competition were sufficiently complex and had implications for the economy of the state of Arizona and, therefore, realistically contemplated the introduction of a plan for retail electric competition in late 1999 -- but not necessarily competition itself. By establishing the first phase of competition to begin in 1999, the Draft Rules fail to consider the Legislature's wishes and are, therefore, premature. The Draft Rules simply put the cart before the horse and do not represent the proper coordination of efforts between the Commission and the Legislature that is essential if retail competition is to be a reality in Arizona.

b) APS IS ENTITLED TO COMPENSATION FOR ANY INVOLUNTARY AMENDMENT TO OR RESCISSION OF ITS CC&N BY THE COMMISSION

Because APS' certificate rights are vested property rights under the Arizona Constitution (*See*, *Trico* and *Tonto Creek Estates, supra)*APS has a constitutionally assured right to compensation before there can be any involuntary rescission or amendment of those rights by the Commission through the introduction of retail access or otherwise. *Loretto v. Teleprompter Manhattan CATV Corp.,* 450 U.S. 419, 102 S.Ct 3164, 73 L.Ed.2d 868 (1982) ("We conclude that a permanent physical occupation authorized by government is a taking without regard to the public interests that they serve. Our constitutional history confirms the rule, recent cases do not question it, and the purposes of the Takings Clause compel its retention."). Taking what is an exclusively owned and operated system and opening it to the beneficial use of other electric providers is no less a physical taking than those dealt with by the line of cases mentioned by the Supreme Court in *Teleprompter*. Nor is the takings argument diminished in any way by the fact that the utility is heavily regulated. *GTE Northwest, Incorporated v. Public Utility Commission of Oregon,* 321 Or. 458, 900 P.2d 495 (1995).

In *Arizona Water Company v. City of Yuma*, 7 Ariz. App. 53, 436 P.2d 147 (1968), the Arizona Supreme Court specifically found that the value of a holder's monopoly certificate rights was part of the "going concern" value of the holder's business for which compensation was legitimately due. Violation of such rights is compensable even if no tangible utility assets are involved. *Sende Vista*

Water Company v. City of Phoenix, 127 Ariz. 42,45, 617 P.2d 1158 (App. 1980); and *Flecha Caida Water Company v. City of Tucson*, 4 Ariz. App. 331,334, 420 P.2d 201 (1966).

In respect to the Draft Rules, a "taking" of a utility's property devoted to retail electric service would include consideration of at least the following four components:

1) loss of the exclusivity of its CC&N's;
2) compelled use of its power lines ("wires") for competitors' benefit;
3) severance damages; and
4) compelled service to customers, who, because of the transition from regulated utility service, the utility no longer has the right to serve.

The Draft Rules do not even purport to address the rights of Affected Utilities to just compensation, nor do they recognize that they constitute an impairment of the contract between these utilities and the state. *In Application of Trico, supra*, the Supreme Court described an electric utility's CC&N as a "contract:"

> By the issuance of a certificate of convenience and necessity to a public service corporation the State in effect contracts that if the certificate holder will make adequate investment and render competent and adequate service, he may have the privilege of a monopoly as against any other private utility.

Application of Trico, supra, at 380-381.

Both the Federal and Arizona Constitutions prohibit government actions that would impair contract rights. *See* U.S. Constitution, Article 1, § 10; Arizona Constitution, Article 2, § 24. Yet the Draft Rules, if adopted, would constitute nothing less that an attempt to impair this legislatively created contract. APS has consistently taken the position that legislative authorization is required before the first kWh of retail wheeling can be authorized or directed by the Commission.

Thus, even if the Commission had the substantive power to amend or rescind the Company's certificate rights in the manner proposed and even if the Commission had followed the prescribed procedures, the Draft Rules would represent an impermissible taking of APS' property without just compensation, as well as a constitutionally impermissible impairment of its contract with the state.

This defect in the Draft Rule is worsened by the fact that Rule R14-2-xxx7 provides absolutely no assurance that prudently incurred costs left stranded by the Draft Rules will be recovered. APS understands that the purpose of regulation is to provide an opportunity for full cost recovery - not a guarantee. However, the costs in question here are not investments idled by errors in forecasting or the vagaries of the economy or imprudencies of utility management. These are costs previously incurred in response to APS' legal obligation under its contract with the state to provide adequate service throughout its certificated area at reasonable rates as set by this Commission. APS and other "Affected Utilities" are legally entitled to an opportunity to recover such costs.

In the President's Economic Report transmitted to Congress in February 1996, the Clinton Administration stated:

> To be sure, utilities should be granted recovery only of costs prudently incurred pursuant to legal and regulatory obligations to serve the public. Investments made after utilities are notified that competition is coming *and are relieved of their obligations to serve* should not qualify; and the utilities must try to mitigate their losses. *But recovery should be allowed for legitimate stranded costs. The equity reason for doing so is clear, but there is also strong efficiency reason for honoring regulators' promises. Credible government is key to a successful market economy, because it is so important for encouraging long-term investments. Although policy reforms inevitably impose losses on some holders of existing assets, good policy tries to mitigate such losses for investments made based on earlier rules, for instance, by grandfathering certain investments when laws and regulations change.* (emphasis added).

Every jurisdiction that has generically addressed this issue has provided stronger assurances of stranded cost recovery than does the Draft Rule. While they might differ in how they treat mitigation offsets (such as allowing only a specified percentage of gross stranded costs in lieu of arguing over specific mitigation measures), none has adopted the ambiguous "wait and see" attitude of the Draft Rules. Moreover, past experience has taught Arizona utilities that when the Commission says it will determine the recovery of this or that cost on a "case by case" basis (*e.g.,* FASB 106 costs, CWIP, CAP costs), the subsequent "case by case" determination is invariably one that denies recovery.

Aside from the potentially devastating financial impact of such disallowance on APS and other "Affected Utilities", the Draft Rules represent a taking of the Company's property just as surely as are the severance damages allowable in a traditional condemnation action in this state. The Commission cannot do by rule what every other political body in Arizona is prohibited from doing without full provision for adequate compensation, by which APS means a reasonable opportunity to recover all investments and costs "stranded" by virtue of the Commission's implementation of the Draft Rules.

c) APS IS ENTITLED TO NOTICE AND AN EVIDENTIARY HEARING BEFORE ITS CC&N CAN BE AMENDED OR RESCINDED

Both *Trico* and *Tonto Creek Estates* hold that a utility's monopoly CC&N is a "vested property right" protected by the Arizona Constitution. In *James P. Paul*, the Supreme Court held that "Because there was no *evidentiary* showing that Paul was unable or unwilling to provide service at reasonable rates, the Commission was without legal authority to amend Paul's certificate as it did." [Emphasis supplied.] *Id.* at 431. In *Tonto Creek Estates*, the Court of Appeals indicated that any attempt by the Commission to amend the rights granted by a CC&N without strict compliance with A.R.S. § 40-252 was "void for lack of jurisdiction." *Id.* at 57. Amendment or rescission of that right is subject to A.R.S. § 40-252, which entitles APS to notice *and an evidentiary hearing* "as upon complaint" - not a "workshop" or a rulemaking proceeding.

Even aside from A.R.S. § 40-252, APS would be entitled to a full evidentiary hearing prior to consideration of the Draft Rules by virtue of A.R.S. § 41-1061. That statute is applicable to any "contested case." A.R.S. § 41-1001(5) defines "contested case" as any case concerning (among other things) "licensing." The term "licensing" is itself defined to include a CC&N. A.R.S. § 41-1001(12).

The Commission's own procedural regulations define the kind of full evidentiary hearing suggested by both the statute and Arizona judicial decisions and the Fourteenth Amendment to the United States Constitution, before the Commission can amend, alter or rescind the incumbent's CC&N. Specifically, A.A.C. R14-3-104(A) grants parties the right to present testimony and cross-examine opposing witnesses. A.A.C. R14-3-109(F) requires that all testimony presented to the Commission be under oath. Inasmuch as the rulemaking process does not provide for this level of procedure, this is further support for the proposition that the Commission cannot do by rulemaking that which can only be accomplished -- assuming prior Legislative directive -- by evidentiary proceedings.

APS has repeatedly urged that there be full evidentiary hearings in this docket prior to any attempted introduction of retail electric competition. This is not only sound policy - a policy universally followed in other jurisdictions considering industry restructuring - but is required by Arizona law, including the Commission's own regulations. The Draft Rules neither provide for such hearings nor are they the product of such hearings, and thus any attempt to enact them would be, in the words of the Court in *Tonto Creek Estates*, "void."

d) THE DRAFT RULES VIOLATE THE RATE REDUCTION AGREEMENT

1. Paragraph 6

Paragraph 6 of the Rate Reduction Agreement approved by Decision No. 59601 (April 24, 1996) prohibits any party from seeking to change rates, except as permitted by the Agreement, before July 2, 1999. Yet the Draft Rules (*e.g.,* R14-2-xxx4) do precisely that - requiring rate reductions, beginning as soon as 1998, for some 25% of the Company's retail load.[1]

2. Attachment 8

In Attachment 8 to the Rate Reduction Agreement, Staff agreed that there were some 30 odd issues presented by retail electric competition. Staff further specifically agreed: "that they [Staff and APS] shall urge the Commission to consider the following issues as the Commission develops its policies regarding restructuring . . ."

Contrary to APS' understanding of that agreement, APS believes Staff has not sufficiently addressed many of the issues identified in Attachment 8, let alone recommended that these issues be considered "as the Commission develops its policies", *i.e., before* retail competition is authorized. For example, the absolutely critical issue of service area rights is not even mentioned, and the compensation issue is expressly to be decided after restructuring has begun - not before as set forth in Attachment 8.

If it is Staff's intent to urge the Commission to consider these issues as the Commission develops its policies regarding restructuring, then the Staff should establish a procedural schedule as described earlier.

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[1] The Draft Rules could remedy this violation of the Rate Reduction Agreement by clearly assuring 100% recovery of stranded costs.

e) THE DRAFT RULES CREATE AN UNREASONABLE AND UNLAWFUL OBLIGATION TO SERVE

Both *James P. Paul* and *Tonto Creek Estates* clearly established that the traditional utility obligation to serve is legally dependent upon the concomitant *exclusive* right to serve. In other words, if there are no exclusive service rights, there can be no exclusive service obligations. The Draft Rule disregards this requirement.

For instance, Draft Rule R14-2-xxx6 would subject only incumbent "Affected Utilities" to this unfair and discriminatory treatment - one that all but guarantees that such utilities will not be able to earn a reasonable return on the fair value of assets devoted to public service, as is required by Arizona law. *Simms v. Round Valley Light & Power Co.*, 80 Ariz. 145, 294 P.2d 378 (1956).

III. APS' Comments on the Draft Rules.

Recommended additions and APS comments are in bold italic format (ex. ***Example***) and suggested deletions are in strikethrough format (ex. ~~Example~~)

APS has reviewed the Draft Rules and presents the following comments, all of which are premised on resolution of the legal issues address in the preceding section. These comments range from concerns on principles that we believe were not sufficiently addressed, to specific wording changes. In several places, APS believes the rules move too slowly or are too cautious in addressing issues (e.g. reliability, reciprocity and stranded costs) while moving too quickly on many other issues without first developing a factual record. APS has also included a proposed alternative to the solar portfolio standard.

R14-2-xxxl. Definitions
In this Article. unless the context otherwise requires:

1. "Affected Utilities" means the following public service corporations providing electric service:

   Tucson Electric Power Company, Arizona Public Service Company, Citizens Utilities Company, Arizona Electric Power Cooperative, Trico Electric Cooperative, Duncan Valley Electric Cooperative, Graham County Electric Cooperative, Mohave Electric Cooperative, Sulphur Springs Valley Electric Cooperative, Navopache Electric Cooperative, Ajo Improvement District, and Morenci Water and Electric Company.

Comments: The definition appears to exclude some Arizona electric PSC's without explanation.

2. "Bundled Service" means electric service provided as a package to the consumer including all generation, transmission, distribution, ancillary and other services necessary to deliver useful electric energy and power to the consumer's residence or place of business.

Comments: The definition of "Bundled Service" should not limit the Company's ability to 'unbundle' the prices for all the services. That is, we must have the ability to apply, as a package, cost-based, functionally disaggregated rates to 'native', full requirements customers.

~~3. "Buy through" refers to a purchase of electricity by an Affected Utility at wholesale for a particular retail consumer or at the direction of a particular retail consumer.~~

Comments: As discussed in R14-2-xxx4.G, APS believes the definition is not necessary.

4. "Standard Offer" means ~~Bundled Service offered~~ ***full-requirements rates available*** to all consumers in a designated area at regulated rates.

Comments: The definition of a Standard Offer should not limit Affected Utilities' ability to offer services priced on an unbundled basis to full-requirements retail customers. Depending on the final

rule and anticipated market structure, the standard rates offered to all customers may be unbundled service pricing.

5. "Stranded Investment" means the ~~verifiable net difference between the value of all the prudent jurisdictional assets under traditional regulation of Affected Utilities and the market value of those assets directly attributable to the introduction of competition under this Article.~~ ***net investments, costs or future obligations prudently incurred ~~in the past~~ for electric services including generation, transmission and distribution, by an Arizona public service corporation for the benefit of retail jurisdictional customers in its service territory which become unrecoverable because of the introduction of competition under this Article. Stranded Investment also includes an Arizona public service corporation's right to compensation for the loss of constitutionally protected property rights in an exclusive service territory as well as compensation due for the loss of exclusive use of its distribution "wires" by others. All investments and costs allowed by the Commission in setting an Affected Utility's rates shall be deemed prudent individually and collectively for purposes of this Article.***

Comments: The Staff proposed definition uses the word "value" in describing "prudent jurisdictional assets." This term is unclear and is a modifier that adds little to the word "prudent." Therefore, the word "value" should be eliminated from the first line. The Staff proposed definition also does not recognize that costs such as fuel contracts, long-term leases, etc., can also be partially or fully stranded. Such contractual obligations are not financial "assets." Therefore, the Staff definition needs to add the word "costs." Also, the Staff proposed definition needs to include "obligations" for future commitments.

The Staff proposed definition does not appear to recognize that this Article permits competition in non-generation electricity services (transmission and distribution). APS believes these are natural monopolies with inherent economic efficiencies. The Company believes it would be inappropriate to create a competitive future where multiple distribution lines would exist within neighborhoods, producing inefficient economics of scale, creating potentially unsightly structures, and compounding environmental issues, and forcing a dramatic increase in the number and geographic specificity of distribution tariffs. Therefore, competition is inappropriate for these services. In addition, virtually no discussion of this issue has transpired in the various task forces, workshops, and written materials the Staff cites as contributing to the content of this Draft Rule. It is critical for the Commission to acknowledge the potential for stranded costs in distribution services, in particular, if the Commission permits "wires" competition in a final rule.

The Staff should be willing to consider further modifications to this definition to include the results of the Arizona Legislature's study of electricity competition inasmuch as this topic has been specifically identified for detailed study by the Arizona Legislature, as well as likely future legislation on the subject.

6. "System Benefits" means Commission-approved utility low income, demand side management, environmental, renewables ***as described in R14-2-xxx9,*** ~~and~~ nuclear power plant decommissioning programs, ***regulatory assets and stranded investment.***

Comments: There is no reason to distinguish Commission mandated low-income programs, DSM programs, etc., from other costs incurred pursuant to regulatory actions. Thus, regulatory assets and stranded investments should be encompassed within the concept of system benefits.

7. "Unbundled Service" means electric service elements provided and priced separately, including such service elements as generation, transmission, distribution, and ancillary services. Unbundled Service may be sold to ultimate consumers or to other suppliers of ***ultimate*** consumers.

8. "Aggregator"- An aggregator is any qualified legal entity who acquires generation services on behalf of several customers and has responsibility for the acquisition, delivery and payment for such services. Aggregators are legally, technically and financially responsible for non-distribution services provided to their contracted customers and complying with any and all legitimate and legal services, terms and conditions required by the transmitting utility (ies), system operators and generation suppliers."

* * * * * * *

R14-2-xxx2. Filing of Tariffs by Affected Utilities.

Each Affected Utility shall file tariffs consistent with this Article by June 30, 1997 to allow retail electric competition in its service territory.

Comments: This section of the Proposed Rule deals with, among other areas, the Affected Utility filing "Standard Offer," "Unbundled Service" and "Buy-through" tariffs, all by June 30, 1997. We believe the proposed deadline is unrealistic, given the scope of the new tariffs and Commission approvals required prior to filing tariffs. We further believe that reviews and discussions by all the interested and affected parties in both formal and informal processes are essential in order to understand the impacts of these various tariff filings upon electrical rates.

The Staffs' proposed rule will require the Affected Utilities to separate their bundled revenue requirements into functional categories, a process involving refunctionalization of assets and direct assignment and allocation of common costs and administrative and general expenses, so that rates can then be redesigned. This is no small assignment and may require extensive modification of current Commission rate setting policies and practices, as well as, presumably, full rate case hearings, each of which are critical to determining the ultimate price to be paid by consumers for their electricity.

To better understand the extensive modifications that will be necessary before any of the required tariffs could be filed, we have categorized the unbundling issues into two sets: 1) objectives and principles that are to be accomplished, and 2) implementation issues necessary to meet the objectives and demonstrate that the tariffs produce authorized revenue targets, and to obtain approval of tariffs under new and existing Commission rules and practices.

Objectives and Principles

Restructuring Objectives

In its Report of the Working Group on Retail Electric Competition (issued 10/5/95, page 7), the Utilities Division identified criteria for evaluating restructuring options:

- *Economic Efficiency*
- *Fairness of Electric Rates, Terms and Conditions*
- *Reliability of Supply*
- *Stability of Investment Environment*
- *Safety*
- *Maintenance and Creation of Jobs*
- *Protection of Environmental Quality*

These criteria should be thoroughly reviewed and assessed during the on-going unbundling and pricing processes to determine whether the resulting behavioral incentives and pricing mechanisms successfully meet these criteria.

Affected Utilities, while striving to achieve those same objectives and design rates which achieve the long-standing rate principles of sound rate design, must also establish prices that allow for "standard offer" services for full requirements service (identified in the Draft Rule as "bundled service" although these standard offers may well be unbundled pricing) and prices and services for partial-requirements service (identified in the proposed Draft Rule as "unbundled service" and "buy-through" service). This means the Affected Utility must design a pricing strategy, which historically has been based on average embedded cost of service, for full requirements customers while simultaneously predicting the impact on revenues of those customers opting for partial requirements. Predicting this impact is critical so that those customers retaining the full requirements service are not unfairly burdened with additional costs attributable from other customers.

Cost of Service Study

The A.A.C. at R14-2-103.A.3.p. specifies that the test year cost of service will be "The one-year historical period used in determining rate base, operating income and rate of return. The end of the test year shall be the most recent practical date available prior to the filing." This Commission has historically ordered that the test year must be very recent to the proposed effective date for new rates. The Proposed Draft Rules appear to change this long-standing practice by requiring rates to be filed June 30, 1997 for implementation January 1, 1999.

In order to properly unbundle costs, and achieve the objectives described above, we believe the test year principles will need to be established during the transition period to full competitive pricing. Alternatives that should be considered include:

- *Historical test year: whether a historical test year is still practical given the proposed phase-in to a competitive market for generation services;*
- *Contemporaneous test year: modify rules to allow for a more contemporaneous test year which might provide for a better measure of cost causation among customers.*
- *Pro forma adjustments: determine what adjustments are consistent with the competitive future;*

- *Migration, aggregation adjustments: determine, if appropriate, forward looking adjustments that may be necessary consistent with the phase-in schedule;*
- *Future test year: modify rules to allow utilities to propose a future test year.*

The process of unbundling costs will also require that existing cost allocation methods be significantly redesigned, with full evaluation of distinguishable cost characteristics such as:

- *Locational/geographic, in that physical location drives a number of cost parameters such as daily and seasonal demand and energy usage, and type of and extent of distribution system necessary to serve the customer, including rural vs. urban, high vs. low customer density, etc.*
- *Electrical service levels, such as voltage service levels, primary line service types, overhead vs. underground, etc.*
- *Market based services, in that the competitive market will require different services from today.*

Once the total functionalized and allocated costs have been established, then the appropriate billing determinants of demand, energy and number of bills must be derived to calculate unit costs of unbundled services. These have historically been the primary bases for determining the rate levels for the various classes of service. However, in order to deal with the costs identified under the System Benefits Charges section of the Draft Rule, new principles will need to be established related to these charges so that the resulting unit costs and rate levels for the various classes of service are equitably impacted.

Revenue Uncertainty

Unbundled rates introduce at least three issues of revenue uncertainty for which principles should be established so that the burden doesn't fall on the "captive customers." The first is whether unbundled rates, particularly offered on an optional basis will, in fact, yield the Commission approved revenue target. This uncertainty results from applying unbundled rates with approximated future year billing determinants on services that may be only roughly known for the historical test year. The second uncertainty stems from the unpredictable response by consumers of new, perhaps complex, rate structures and a pronounced shift in rates from energy based revenue recovery (¢/kWh) to capacity based recovery ($/kW) for generation and wires capacity. The third uncertainty is the impact of optional rate selections by consumers that will erode revenues when customers make choices to select a rate that lowers their electric bill.

An equally important financial impact, perhaps only indirectly related to unbundling rates, is that the instability and unpredictability of future revenue streams, without the assurance of recovery, could materially increase the utilities financial market risk in the view of rating agencies, and therefore, potentially drive up its cost of capital.

One alternative to deal with the potential instability and unpredictability of future revenue streams would be to include in the Proposed Draft Rule a provision for periodic changes to rate design levels for unexpected results from the restructuring and rate unbundling.

Other Policies

Establishment of the objectives and principles of market restructuring will facilitate the necessary modifications to other related policies such as the extension policy and the terms and conditions of electrical service, both of which are critical to insure a proper unbundled rate design.

Although the general principle of economic feasibility, that is, new construction must meet the Company's authorized rate of return, is anticipated to the basis for extensions, changes in obligation to serve, unbundled services, and cost of service must be reflected in the extension policy and APS' Schedule #3 so that the amounts paid by customers are administered fairly without undue discrimination.

APS currently has eight schedules that specify the terms and conditions of service, other than rates for electric sales, to comply with the A.A.C. rules and regulations, R14-2-201 through 211. Each of these schedules will need to be thoroughly evaluated to determine what changes may be necessary to be reflective of the Draft Rule.

Implementation Issues

In addition to the objectives and principles, other modifications to the rate setting process will be necessary to implement the Draft Rule. The introduction of new and unbundled services will introduce a wide array of issues that will drive the practical issues generally addressed in traditional rate proceedings. These include:

- ***Customers' perspectives of rates (understandability, acceptability, certainty, continuity, convenience of payment)***
- ***Administration (training, plans for administration, support staff, etc.)***
- ***Metering***
- ***Billing systems***
- ***Third party payment arrangements***

The introduction of many new services to customers and new suppliers of generation will require evaluation and the establishment of new policies, procedures, practices and information processing systems. The costs of these activities and the impact on consumers will need to be properly considered in establishing and filing the new rates. Clearly, exploration and further understanding of the implementation issues may serve to guide the judgment of the Commission, Affected Utilities and other suppliers in regards to balancing the complexity of unbundled rates with the ease and cost of implementation and administration.

The gathering and analysis of data and supporting systems necessary to the design of the new tariffs are formidable implementation issues also. For example, load data (timed demand and timed energy) for the proposed rate offerings and unbundled services will be necessary to the calculation of the billing determinants. Accounting data on net depreciated distribution system assets by specific geographic locations will also be necessary. Major functional systems that will require modification and/or creation include billing determinant retrieval programs, load simulation

models, revenue requirements models, trial rate level models, and internal accounting and operational reporting systems.

* * * * * * *

R14-2-xxx3. Certificates of Convenience and Necessity.

A. Any company ***including an Affected Utility*** intending to supply services described in Subsections R14-2-xxx5 or R-14-2-xxx6, other than wholesale generation services ***and other services subject to FERC jurisdiction***, and which would hereby become subject to Commission Jurisdiction, shall obtain a Certificate of Convenience and Necessity from the Commission ~~(unless the company already has an applicable Certificate)~~ ***pursuant to this Article. However, an Affected Utility does not need to apply for a CC&N for any service currently provided within its present service area.***

Comments: The only procedural mechanism under the Draft Rules to obtain a "competitive" CC&N allowing service within an "Affected Utility's" territory is under R14-2-xxx3. Yet that Draft Rule is, by its own terms, inapplicable to incumbent "Affected Utilities" already possessing a CC&N. This would arguably prevent one "Affected Utility" from competing in the service area of another "Affected Utility." APS believes this is certainly an unintended result and suggests the above changes.

This language would also clarify that the Commission is not and presently can not extend its jurisdiction to encompass non-PSCs such as Arizona municipalities or federal agencies.

Salt River Project ("SRP") and other municipal electric utilities are exempt from Commission jurisdiction by virtue of Article 15, Section 2 of the Arizona Constitution. **Rubenstein Construction Co. v. Salt River Project Agricultural Improvement & Power District,** ***76 Ariz. 402, 265 P.2d 455 (1954). To the extent that Draft Rules R14-2-xxx3*** or ***R14-2-xxx11 would authorize SRP or any other non-PSC's to provide service within the certificated territories of "Affected Utilities" under a CC&N obtained from the Commission, such rules represent an unlawful attempt to extend Commission jurisdiction over entities specifically exempted by the Arizona Constitution or which are exempt as a matter of federal law*** **(e.g., *tribal utilities and federal power marketing agencies).***

Aside from the Commission's general lack of authority to implement retail electric competition and its specific inability to regulate non-PSC's, the Staff's attempt to include municipal utilities within the scope of this rule (or R14-2-xxx11) must fail for yet another reason. In Arizona, municipal utilities are prohibited by A.R.S. § 9-516 from providing service within a PSC's CC&N without paying full compensation, including "severance damages" **(e.g., *"stranded investment").*** **Sende Vista Water Company, Inc. v. City of Phoenix,** ***127 Ariz. 42, 617 P.2d 1158, 1161 (Ct. App. 1980). It is interesting to note that A.R.S. § 9-516 was specifically amended to legislatively overrule a contrary holding in City of Tucson v. Polar Water Co.,76 Arizona 126, 259 P.2d 561 (1953).***

Tucson Polar ***had held that municipal utilities were not subject to the provisions of A.R.S. §40-281, et seq., prohibiting competition with PSC's. The Court further indicated that the Legislature was the appropriate body to determine the scope of PSC service area rights. Within two (2) months, the Legislature accepted the Court's invitation and moved forcefully to plug this "loophole" in the state's policy of regulated monopoly.***

A similar prohibition in A.R.S. § 30-315 (a) affecting electric and power districts was upheld as a valid exercise of legislative power in In Re Cabeza Power District, 17 Ariz. App. 414, 498 P.2d 488(1972).

SRP presents yet another unique problem under the Draft Rules. The Commission has several times specifically approved the territorial allocation agreement between the Company and SRP. This territorial agreement prohibits the very sort of reciprocal competition envisioned by Draft Rule R14-2-xxx11. Moreover, the term of that specific territorial agreement is perpetual, is binding upon any SRP "affiliate" and there are no provisions for termination.

As discussed in APS' comments to Draft Rules R14-2-xxx5 and R14-2-xxx6, the Company strongly believes that distribution ought to remain a regulated monopoly service and would only support legislative changes to A.R.S. g40-281, et seq., that preserve that status. The competitive CC&Ns granted by the Commission pursuant to this Article should clearly be limited to jurisdictional generation services.

B. Any company desiring such a Certificate of Convenience and Necessity shall file with the Docket Control Center the required number of copies of an application. In support of the request for a Certificate of Convenience and Necessity, the following information must be provided:

1. A description of the electric services which the applicant intends to offer.
2. The proper name and correct address of the applicant, and
   a. The full name of the owner if a sole proprietorship,
   b. The full name of each partner if a partnership,
   c. A full list of officers and directors if a corporation, or
   d A full list of the members if a limited liability corporation.
3 A tariff for each service to be provided that states the maximum rate and terms and conditions that will apply to the provision of the service.
4. A description of the geographic areas to be served, provided that these areas are restricted to geographical areas served by the Affected Utilities as of the date this Article is adopted and to service areas added under the provisions of Subsection R14-2-xxx1.
5. Appropriate city, county and/or state agency approvals.
6. A description of the applicant's technical ability to obtain and deliver ***a reliable supply of*** electric~~ity~~ ***generation*** and ***all required ancillary*** ~~provide any other proposed~~ services.

Comments: This change reflects both the limitation of competitive CC&Ns to the provision of generation services but makes reliability an important criterion in evaluating new competitive suppliers.

7. Documentation of the financial capability of the applicant to provide the proposed services, including the most recent ***audited*** income statement and balance sheet, the most recent projected income statement, and other pertinent financial information. ~~Audited information shall be provided, if available.~~

Comments: In all instances, the financial information submitted should be audited and verified before the CC&N is granted to ensure the Commission that the financial data submitted accurately presents the true financial condition of the applicant for a certificate of convenience and necessity.

8. A description of the form of ownership (e.g., partnership, corporation).

9. A detailed description of the degree to which the Applicant has provided or is willing to provide for competition within its existing service area (if applicable) or for its existing and future customers.

Comments: This informational provision does not establish reciprocity as a per se requirement (as is imposed on in-state entities) for out of the state providers, but would permit the Commission to consider the lack of the impact of reciprocal opportunities when evaluating generation suppliers authorizing a new certificate of convenience and necessity.

In Attachments 8 and 9 to the Rate Reduction Agreement, as well as in its comments of June 28th in this Docket, the Company has stressed continually the critical importance of creating meaningful and comparable reciprocal opportunities for incumbent Arizona providers and has insisted that the Commission provide for reciprocity(through legislation if necessary) before authorizing any competition. Competition ought not to be a "one way street."

~~9~~*10.* ~~An Arizona~~ business plan. ~~; if this information is confidential, the~~ ***Such*** plan ~~may be submitted only~~ ***shall be considered confidential and shall be submitted solely*** to ***Commission*** Staff ~~and need not be filed in Docket Control~~ ***under separate cover.***

Comments: Requiring the submittal of an Arizona business plan appears at odds with the direction the Staff is taking in the Draft Rules. Notwithstanding confidential assurances, data of this nature that goes to competition for retail electric service should not be disclosed to competitors and is needlessly placed "at risk" once filed with the Commission. However, the information is to be filed, nonetheless, the regulation should at least grant per se confidentiality to such data. Additionally, not all market entrants will have a specific Arizona Plan, but rather an overall company plan; therefore, Arizona should be deleted.

~~10~~ 11. Such other ***relevant*** information as the Commission or the Staff may request.

C. At the time of filing for a Certificate of Convenience and Necessity, each applicant shall notify the Affected Utilities in whose service territories it wishes to offer service of the application. Rule shall specify form and manner of notice.

D. The Commission may deny certification to any applicant who:
   1. Does not provide the information required by this Article.
   2. Does not possess adequate technical or financial capabilities to provide the proposed services.
   3. Fails to provide a performance bond, if required.
   4. Does not demonstrate that certification is in the public interest.
   5. Is unwilling or unable to provide for meaningful and comparable reciprocal opportunities within its existing service area to Affected Utilities.

E. Every company obtaining a Certificate of Convenience and Necessity under this Article shall obtain certification subject to the following conditions:

1. The company shall comply with all Commission rules, orders, and other requirements relevant to the provision of electric service and relevant to resource planning.
2. The company shall maintain accounts and records as required by the Commission.
3. The company shall file with the Director of the Utilities Division all financial and other reports that the Commission may require and in a form and at such times as the Commission may designate. ***Such information shall be deemed confidential unless otherwise ordered by the Commission after notice and hearing.***
4. The company shall maintain on file with the Commission all current tariffs and any service standards that the Commission shall require.
5. The company shall cooperate with any Commission investigation of customer complaints.
6. Failure to comply with any of the above conditions may result in recision of the company's Certificate of Convenience and Necessity.

F. In appropriate circumstances, the Commission may require, as a precondition to certification, the procurement of a performance bond sufficient to cover any advances or deposits the applicant may collect from its customers, or order that such advances or deposits be held in escrow or trust.

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R14-2-xxx4. Competitive Phases

Comments: Achieving a retail choice phase-in schedule that results in a fair, efficient and reliable transition to a competitive generation market is, perhaps, the most challenging aspect facing Arizona in restructuring the electricity service industry for competition. APS recognizes that its proposed phase-in schedule contained in the Arizona Customer Choice Plan may not be perfect. Moreover, any schedule should be reasonably flexible so that it can be modified to incorporate events as they unfold. The ACCP's schedule is a good faith best effort on APS' part to effectively balance the myriad of technical, regulatory, legislative, customer, safety and utility financial issues and concerns that come forth in any schedule to implement retail choice. Briefly, listed below are the primary advantages of APS' proposed schedule to begin a phase-in of retail choice on or about the year 2000 for the largest electricity consuming customers and subsequently progressing on or about 2004 to residential consumers.

Primary Advantages of APS' Retail Choice Phase-in Schedule

1. The opportunity for successful mitigation of stranded investment costs is improved for Affected Utilities by a more extended reliance on performance based pricing.

2. Arizona can learn greatly from even the small number of other states that are presently more focused than Arizona on developing the institutional architecture of wholesale electricity competition. A national debate is occurring right now in the states and at the FERC regarding these issues. By waiting to benefit from this complex process, Arizona can avoid some very costly

mistakes. Arizona should select from the best of the practices and procedures implemented and proven elsewhere.

3. Arizona customers will benefit from experience with the unbundling of services and prices prior to exercising choice. Unbundling of prices and services can progress from informational, or "shadow", billing to actual unbundling of full requirements tariffs and ultimately to the unbundling of partial requirements tariffs under retail choice. Unbundling presents numerous issues resulting from starkly different rate structures and, therefore, has the potential to create winners and losers in ways and to degrees neither anticipated nor intended.

4. By focusing on unbundling issues, rather than on wholesale institutional architecture issues, Arizona can establish a true leadership role as other states have given this category scant attention to date.

5. Inasmuch as APS believes stranded cost recovery is essential to this process, resulting overall price reductions to customers from retail choice will be moderate for some years to come and shall result from improvements in efficiency of utility operations. Given the very real risk that unbundling electric services and prices will increase bills more than the efficiency gains for a large number of customers, a deliberate course for unbundling is necessary and under appreciated elsewhere.

6. Retail choice will require significant new and expensive infrastructure to be successful. APS' phase-in plan in the early years, confines needed infrastructure expenses to metering and communications. This is because APS' plan limits the increase in retail choice transactions to an amount manageable by existing system-wide informational, scheduling and coordinating capabilities. The Staff's 1999 requirement of 20% choice exceeds the existing transactional capabilities of Affected Utilities and is roughly comparable to the requirements of APS' proposed schedule for the year 2002. APS' preference is to front load the cost savings for customers through use of PBR and back load the expenses necessary to fully implement an architecture for competition.

7. Although some very large retail customers are aware that retail choice may reduce their electric bills, it is fundamentally a supply driven initiative. In general, the majority of customers are presently vastly unaware in the present debate. This offers a unique opportunity to get it right. APS' plan allows those few customers actively seeking alternatives to have choices at an early date.

8. APS' schedule more closely comports to the schedule contained within the Arizona Legislature's study bill on electricity competition. Given their important legal policy and economic development responsibilities in Arizona, their input is mandatory.

Staff's proposed phase-in plan simply does not present the same advantages listed above. Moreover, the singular "advantage" of the Staff's proposal over that of the Company, the early inclusion of residential and small commercial customers in retail competition, is presumably based on concerns that such customers would otherwise be cut out of any benefits of competition or worse yet, be forced to bear a disproportionate amount of the costs stranded by the departing larger customers. Yet, APS' plan does neither of those.

A. Each Affected Utility shall make available at least 20 percent of its 1995 system retail peak demand for competitive generation supply to all customer classes (including residential and small commercial consumers) by January 1, 1999.

1. No more than one-half of the eligible demand may be procured by consumers whose individual contract demand is greater than 3 MW each.

Comments: It is unclear as to how Staff is defining demand. Staff's reference to system peak demand infers coincident peak (CP) demand. APS suggests that any references to demand be specific as to whether a CP or noncoincident (NCP) demand is meant.

Assuming the amount of retail load for competitive generation supply is premised on system peak (i.e. CP) demand then complying with Staff's pro rata class phase-in plan is problematic when it comes to all customers without demand interval meters. Most APS customers are not billed on meters with demand capabilities. Without a new metering system, it will not be possible to tell when the targeted per cent of load has been met.

2. At least 10 percent of the eligible demand shall be reserved for residential consumers.
3. Aggregation of loads of multiple residential, commercial, or industrial consumers shall be permitted.

Comments: We believe there is a need for clarity surrounding the definition of the term aggregator. For this reason APS has provided a definition in section R14-2-xxx1. It is unclear if any individual aggregated consumer group which includes residential customers either exclusively or in combination with other classes would be eligible to secure the entire residential allocation (i.e. 10% or 20% as called for) and exclude other participants. This point is especially valid if the affected utility elects a first-come, first-served selection method under the provisions of R14-2-xxx4, E.1. Such potentially discriminatory results represent issues that must be addressed in order to support a phase in plan based on a percentage of each class.

B. Each Affected Utility shall make available at least 50 percent of its 1995 system retail peak demand for competitive generation supply to all customer classes (including residential and small commercial consumers) by January 1, 2001.

1. No more than one-half of the eligible demand may be procured by consumers whose individual contract demand is greater than 3 MW each.
2. At least 20 percent of the eligible demand shall be reserved for residential consumers.
3. Aggregation of loads of multiple residential, commercial, or industrial consumers shall be permitted.

Comments: A 50 percent requirement raises numerous system issues. The operation of an electric grid requires the simultaneous matching of generation sources with instantaneous fluctuations in demand. These extraordinarily complex tasks require very sophisticated computer systems and very close coordination among dispatch centers. At the present ,little consideration has been given to any detailed procedures and systems necessary to allow a very large number of buyers and sellers to actively participate in the market for electricity. Important activities such as scheduling of transactions and after-the-fact settlements are complicated exponentially as more and more

participants enter the market. Scheduling requires hourly analysis of control area activities for prescheduling on a 24 hour and real time (i.e., next hour) basis and for reconciling billing after the fact. The existing volume of current transactions involves 20 utilities and marketers with over 200 transactions. The current system software and manpower capabilities are capable of handling approximately 1500 transactions. An expansion of the current system including the current system to accommodate the expected explosion in volume of transactions is not feasible, nor does the technology exist to meet these expanded requirements. It would behoove Arizona to allow the technology to be more fully developed prior to experimenting here.

Necessary billing process enhancements also present the industry with technological and timing challenges. In addition to resolving policy and logistical issues such as the treatment of partial payments, establishing the creditworthiness of new hook-up customers, disconnect and reconnect responsibilities, the handling of bill inquiries etc., changes and enhancements will be required to existing customer information and billing systems. Among these are: the ability to identify energy service supplier(s); ability to bill on behalf of various suppliers, as well as rebill, correct bills, work exception bills; ability to account for energy and revenues for other suppliers; accommodate an expanded number of unbundled and bundled rate structures and different billing formats; provide for credit and collection services, partial payments, disconnection and collection notification.

A metering and communication system is necessary for developing the load profiles to forecast next day (and even next hour) energy needs and corresponding generation schedules, measuring actual use, and reconciling and assigning actual use to each hour of billing must be developed. This will require real-time meters capable of recording energy consumption on an hourly basis instead of the current monthly basis.

Although the use of imputed average load curves based on relatively small samples of "typical" customers to estimate hourly demands may or may not prove adequate for scheduling purposes, the inability to accurately reconcile hourly generation schedules to hourly demand served by a third party after the fact requires the aggregator to ration during shortages or places the local operating utility, (and ultimately other consumers) in the position of absorbing any differences in costs. Without an hourly comparison of third party delivered energy and actual demand, the energy cost incurred by the operating utility in automatically making up any differences (by virtual of its area control responsibilities) cannot be determined and charged back to the third party.

The nation can expect an overwhelming demand for metering/communication products. At present, there is no agreement on a common communication protocol for delivering, receiving, interpreting and initiating responses to pricing and metered data. APS estimates the cost to be in the approximate range of $230 million (or approximately $110 per customer) for a rudimentary statewide communication and metering system capable of hourly load monitoring. A requirement for "instantaneous" metering capability such as that required for system regulation would at a minimum triple this estimate to approximately $700 million (or approximately $330 per customer).

On the customers' side of the meter, those customers wishing to take advantage of real time pricing and unbundled services could collectively incur equipment costs which could add an additional $300 million to well in excess of $1 billion ($150 to $800 per customer). The majority of these expenses would be incurred by the residential customers.

C. Prior to 2001, no single consumer shall receive more than 20 percent of the available kW in a given year in an Affected Utility's service territory.

D. Each Affected Utility shall make available all of its retail demand for competitive generation supply by January 1, 2003.

E By the date indicated in Subsection R14-2-xxx2, Affected Utilities shall propose for Commission review and approval how customers will be selected for participation in the competitive market prior to 2003.

1. Possible selection methods are first-come, first-served, random selection via a lottery among volunteering consumers, or designation of geographic areas.

Comments: No phase-in plan pleases everyone. Note that a phase-in plan based upon a percentage participation across all classes will have the effect of creating the perception of unfairness and discrimination and can be expected to result in a high number of customer complaints. A participation selection process based upon geographic area may be appropriate given technical considerations, but could create a perception of an unlevel playing field between cities. Businesses in a city not selected to participate may claim an economic disadvantage over those not selected. Additional issues will arise under any phase-in from a natural customer churn. Experience indicates that about one-third of APS customers disconnect and re-connect in a year. Many of these customers are moving. Will competitive eligibility move with them? Will the new owner automatically succeed to that eligibility (whether that owner wants to or not)?

A lottery has its detractors as well. It allocates by "luck". The less aware may not submit their applications for participation. As with the geographic option, competitive advantage perception issues may also arise. There could easily be two similar businesses across the street from each other having differing eligibility.

APS requests that the above considerations be weighed in any proceeding to determine the optimal phase-in with customer choice being the driver for whatever method is chosen.

2. The method for selecting customers to participate in the competitive market must fairly allow participation by a wide variety of customers of all sizes.

Comments: Before direct access can be implemented, APS believes it is very important that an extensive consumer education effort be undertaken to insure the benefits of retail access are optimized by an informed populace interacting effectively with multiple energy service providers and to limit opportunities for abuse. This is no less daunting a task than the task faced by the industry in transforming the marketplace for DSM services, a process which many in the industry project to take 3 to 5 years of intensive educational efforts.

There is currently a low level of awareness of what retail access is among the general public. Only recently has any information been disseminated in the popular press. We believe that consumers are not interested in wanting to learn about complex issues or deal with low involvement categories. Similar apathy characterizes the DSM marketplace. We can, therefore, expect that it will take a very significant and intensive educational effort to overcome the level of apathy and lack of knowledge which currently exists.

Without a significant educational effort, either the eventual benefits of retail access will be untapped by the general mass of utility customers and/or the availability of competitive choices could potentially be chaotic and result in increased customer complaints. As was seen with the deregulation of the telephone industry and as evidenced by the practice of "slamming" which followed, the potential for poor customer choice and consumer fraud is very real, even concerning a service (long distance calling) that consumers understand far more the electricity. Thus, any phase-in approach will require that all consumers be educated since all will be impacted and will demand information on the restructuring of the industry.

3. All customers who produce or purchase at least 10 percent of their annual electricity consumption from photovoltaic or solar thermal resources installed in Arizona after January 1, 1997 shall be selected for participation in the competitive market if those customers apply for participation in the competitive market ***provided that participation levels have not already been met and the participants have not already been selected.***

Comments: It is unclear as to whether customers who produce or purchase 10% of their energy from solar resources will be counted toward achieving the established class quotas. APS suggests that they should be.

F. Consumers served under existing contracts are eligible to participate in the competitive market prior to expiration of the existing contract only if the Affected Utility and the consumer agree. Failure to reach agreement is not a basis for Commission action.

Comments: The ACC should set a policy that it will not consider complaints filed by customers that are motivated by a desire to void their contractual obligations with Affected Utilities.

G. Buy-throughs.

Comments: Within the phase-in plan proposed above, no interim program is necessary and the buy-through provision should be deleted. All Affected Utilities currently have the ability to seek Commission approval for offering pricing options prior to retail access.

Additionally, APS would also object to allowing the customer to directly contract with other suppliers. APS must act as the agent in order for the transaction not to become an unbundled, "buy/sell" retail wheeling transaction.

The Federal Energy Regulatory Commission has made the following statement in its Notice of Proposed Rulemaking promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities[2] regarding jurisdiction over what it calls "buy-sell" transactions:

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[2] Docket No. RM95-8-000 (March 29, 1995) at pages 99-100. This position was affirmed in the Commission's Order No. 888 issued April 24, 1996 in Section IV.I.

Finally, we address a specific type of retail service that we believe to be "bundled" retail service in name only: a so-called "buy-sell" transaction in which an end user arranges for the purchase of generation from a third-party supplier and a public utility transmits that energy in interstate commerce and re-sells it as part of a "bundled" retail sale to the end user. We have determined that in these types of transactions the retail "bundled" sale is actually the functional equivalent of two unbundled retail sales: (1) a voluntary sale of unbundled transmission at retail in interstate commerce, subject to our exclusive jurisdiction;[187] and (2) a sale of unbundled generation at retail, subject to the state's jurisdiction.... For these types of sales, public utilities will have to provide the voluntary retail transmission component of the sale under a FERC-filed tariff consistent with the substantive requirements of this proposed rule.

Footnote 187 stated, "As discussed infra, there would be a component of local distribution in such a transaction, subject to the state's jurisdiction."

Currently, it is unclear what deference the FERC will allow to states on what is considered "local distribution facilities." The FERC will generally exercise jurisdiction over a local distribution company's facilities based on the assessment of the transfer capability. If the loadings or an outage of a local distribution company's facilities has a significant impact on transfer capabilities, the FERC may exercise jurisdiction regardless of voltage. In addition, the pricing of ancillary services to a retail customer must be consistent with FERC order 888 as demonstrated by the FERC's response to the New Hampshire Retail Access Pilot program. Until the definition of APS' local distribution facilities is determined, it is impossible to submit tariffs for distribution rates to the ACC, as distribution plant is simply unknown.

~~1. Each Affected Utility shall file by the date indicated in Subsection R14-2-xxx2 a mechanism which enables all classes of its customers to engage in a Buy-through, including customers who wish to use the Buy-through mechanism to obtain electricity from photovoltaic or solar thermal generating resources.~~

~~2. Buy-throughs shall be permitted as early as January 1, 1998.~~

~~3. Each Affected Utility shall make at least 5 percent of its 1995 system retail peak demand available for competitive procurement under this Buy-through mechanism.~~

~~4. The Affected Utility shall permit customers to identify electricity sources which the Affected Utility would obtain on behalf of the customer and provide to the customer at unbundled rates described in Subsection R14-2-xxx6, below, plus the cost of the electricity plus a mark-up on the cost of electricity not to exceed 15 percent of the cost of the electricity.~~

~~5. Buy-throughs shall not be considered as meeting the requirements of Subsections R14-2-xxx4(A), R14-2-xxx4(B), or R14-2-xxx4(D).~~

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R14-2-xxx5. Competitive Services

A. A properly certificated electric company may offer any of the following services under bilateral or multilateral contracts ~~with~~ ***to retail*** consumers ***eligible to receive competitive services in the timetable set forth in R14-2-xxx4***:

1. Distributed ~~energy~~ services ***generation*** at market based rates (serving one or more consumers located in proximity, and not ~~necessarily~~ requiring transmission ***or distribution*** service from others ***to effect the transaction***).

Comments: This addition is necessary to properly define distributed energy. Insofar as the customers of distributed generators require other services (e.g., back-up generation), these are separate transactions.

2. ***Direct retail sale of*** central station generation ~~services~~ at market based rates ~~(generation serving~~ to one or more ***retail*** consumers located at a distance from ~~consumers~~ ***the generation station(s)*** and requiring transmission service, ~~some~~ ancillary services~~,~~ and***/or*** ~~possibly~~ distribution service).

Comments: This clarification is necessary to make it clear that the sales intended to be covered are Arizona jurisdictional direct retail sales.

~~3. Combinations of distributed and central station generation services.~~

Comments: Appears redundant and added in its place is the ability for energy merchants to sell at retail. No other section of the Draft Rules appears to permit retail sales other than from generation owned by or under contract to the seller.

3. Retail sale of energy services purchased from wholesale generators.

4. For purposes of this Article, an Affected Utility seeking to serve customers outside of the area covered by its current CC&N or customers eligible for competitive generation supply within its current CC&N, will be treated the same as other companies seeking to provide retail service at market rates.

B. A ***properly certificated electric*** company ~~other than an Affected Utility~~ ***may*** provide services described in Subsection R14-2-xxx6***, except distribution, metering and certain ancillary services*** after filing appropriate tariffs and receiving commission approval of those tariffs.

Comments: Setting aside the previously discussed lack of legal authority of the Staff's proposed order, APS believes it is unwise to introduce competition for distribution, metering services and other ancillary services (R14-2-xxx6.C1, -xxx6.C..2, and -xxx6.C.6) until after fully completing the transition to retail generation competition, if at all. These references present an entirely new array of heretofore unmentioned and unresolved issues concerning distribution construction , operation, and maintenance, pricing and local franchises for the use of public rights-of-way. For instance, is the customer group eligible to receive competitive distribution service the same group of customers eligible for generation competitive service or some altogether different group. It appears the latter, yet this would produce a varying mixture of eligibility for differing competitive and regulated services.

The Draft Rule does not address many of these new issues nor does APS' proposed language revisions to the Draft Rule fully recommend the many necessary changes distribution competition

would entail. Virtually no discussion of this issue has transpired in the various task forces, workshops and written materials the Commission cites as contributing to the content of this Draft Rule.

Nevertheless, APS has proposed modified language to this section to insert, for clarity, that the services we believe the Staff intended are those enumerated in R14-2-xxx.6.C. Also, the language was changed to not exclude Affected Utilities seeking to compete outside of their territories.

* * * * * * *

R14-2-xxx6. Services Required To Be Made Available by Affected Utilities

A. Until ~~the Commission determines that competition has been substantially implemented~~ each Affected Utility shall make available to all consumers in its service area, as defined on the date indicated in Subsection R14-2-xxx2, Standard Offer bundled generation, transmission, ancillary, distribution, and other necessary services. ~~at regulated rates.~~

~~1. An Affected utility may request that the Commission determine that competition has been substantially implemented to allow discontinuation of Standard Offer service and shall provide sufficient documentation to support its request.~~

~~2. The Commission may, on its own motion, investigate whether competition has been substantially implemented and whether Standard Offer service may be discontinued.~~

Comments: By ordering retail competition into the service area of an Affected Utility, the ACC has unilaterally modified the incumbent's obligation to serve. A substantial aspect of the regulatory compact underlying the certificate of convenience and necessity is the promise on the utility's part to operate and maintain sufficient resources to serve the needs of consumers in the certificated service area at reasonable rates. [Application of Trico Electric Co-operative, Inc., 92 Ariz. 373, 377 P.2d 309 (1962); see, also, Electrical District No. 2, Pinal County, Arizona, v. Arizona Corporation Commission, 155 Ariz. 252, 745 P.2d 1383 (1987)] Introduction of retail competition into the service area results in an imbalance in this respect. The incumbent utility now is faced with an oversupply of resources that it must nevertheless maintain in reserve under its obligations established by the certificate. Therefore, a quid pro quo is required to maintain an equitable balance. In other words, assuming the appropriate process is followed to introduce retail competition into the marketplace, the incumbent utility should be freed of its obligation to serve customers who elect to purchase their services elsewhere. Incumbents should not be required to provide back up or standby services if the customer's elected provider fails to perform. That is a risk the customer must take. The incumbent's obligation to provide backup or standby services for a consumer who has elected to obtain its service elsewhere, should not be provided at standard rates, but at a rate set that compensates the utility for the resources reserved for that customer and that fairly reflects the nature of the service.

This being said, the changes suggested above represent a compromise position by providing for a standard offer until a specific date certain. It also allows Affected Utilities to avoid being locked into a "lower of cost [i.e., standard offer] or market" position for that portion of its load eligible for "competitive supply."

B. ***Rates for Full Requirements Service***

1. By the date indicated in Subsection R14-2-xxx2, each Affected Utility may file proposed tariffs to provide Standard Offer ~~Bundled~~ ***Full Requirements*** Service and such rates shall not become effective until approved by the Commission. If no such tariffs are filed, rates and services in existence as of the date in Subsection R14-2-xxx2 shall constitute the Standard Offer ***Full Requirements Service.***
2. ***Such rates shall, at a minimum, reflect costs of providing the services.***

Comments: Distribution costs and prices will need to be de-averaged or unbundled simultaneously with retail choice commencing in order to eliminate existing cross subsidies because:

1) Unbundling of generation eliminates generation subsidies of other services (including distribution), thereby likely making many existing customers unprofitable for the remaining regulated services they receive.
2) Failure to act at the start of retail choice eventually means substantial distribution rate increases for many customers following generation related rate decreases (i.e. bad pricing signals).
3) Affected Utilities would be exposed to loss of existing distribution services to municipalization if costs are not more closely reflective of the actual costs to serve specific geographic areas.

Although work is progressing at APS, nothing conclusively identifies the "payers" and "recipients" of both generation and distribution subsidies. However, it is likely that de-averaging or unbundling will produce positive and negative impacts for customers along at least the following dimensions: a) rural vs. urban customers; b) low vs. high usage customers and c) low vs. high load factor. FERC has through its case law taken an extreme position on this issue. They are relying on a "direct assignment" method of allocating distribution cost. This approach is the ultimate in unbundling costs and basing prices thereupon in that customers literally pay for the specific facilities they rely on for service.

Clearly, low usage, low load factor, rural customers would face price increases from de-averaging of distribution costs and prices. It is unknown whether eventually reductions in generation prices from competition will be enough to offset distribution price increases for these customers. In other words, overall rates may increase for these customers as a result of competition.

As noted in the comments on unbundling, closely related issues concern the extension policy. Extension policies relate to the terms and conditions of providing electric facilities to new customers. In Arizona's high growth economy, extension policies are important to economic development. However, in order to avoid creating any new distribution subsidies, Affected Utilities would need to revise extension policies to ensure that new customers always pay their costs. It is expected that revised policies would result in greater up front costs to new customers relative to the present. Anticipated changes to the existing extension policy include:
1. Elimination of all generation, and perhaps transmission, costs and revenues from extension policy revenue requirements calculations. In other words, extensions would have to achieve the required rate of return on the basis of projected distribution revenues versus distribution cost. (This change effectively eliminates generation subsidies of new customers referred to above.)

2. Reduction in capital recovery periods. Presently, investment costs to serve new customers are based upon recovery over periods of 30 to 40 years. However, given the Draft Rule and the already existing potential uncertainty of full costs recovery via PBR for wires services, a significant shortening of recovery time horizons (say, 15 years), as is typical for competitive companies, is necessary.

3. Residential real estate extensions under the revenue or economic feasibility basis should be based on estimated usage for the actual appliance fuel mix, not based on an all electric usage assumption.

4. The footage basis may need to be eliminated and revenue basis criteria would need revisions to appropriately recover unbundled service costs.

C. By the date indicated in Subsection R14-2-xxx2, each Affected Utility shall file Unbundled Service tariffs to provide the services listed below to all eligible ***partial requirements*** purchasers on a nondiscriminatory basis.

Comments: It should be noted that the ACC's jurisdiction over retail wheeling services is limited as a result of FERC's Order 888 findings.

1. Distribution service.

Comments: FERC Order 888 does defer to the ACC over "local distribution facilities." However, as yet, there has been no bright line regarding identification of exactly what facilities constitute "local distribution facilities."

For wholesale customers that require the use of distribution facilities in order to effect open access transmission service, FERC has asserted jurisdiction over pricing for the use of such basis whereby the customer is allocated (specifically assigned) the costs of their proportionate share of those local distribution facilities utilized to effect service. This requires that a facilities study be conducted for each affected customer in order to identify those local distribution facilities and the cost of such facilities.

Because such studies are generally time consuming and costly to perform, it would be impractical to require such a methodology for service to a significant number of retail customers. APS currently believes that utilization of any existing distribution facilities by retail wheeling customers should be charged based on rates developed pursuant to an allocation of the embedded costs of pertinent distribution facilities rather than the direct assignment methodology.

The Draft Rule is moot with regard to what the utility's obligation is when local distribution facilities must be upgraded in order to effect service or when new distribution facilities are required. If the Affected Utility is required to install local distribution facilities, the cost responsibility for such facilities should clearly be that of the customer. This is exactly what FERC requires for wholesale entities that require distribution facilities.

Additionally, by requiring that customer who actually causes the new facility or upgrade to be installed to bear the cost, the utility's other customers are not subsidizing service to said customer and are in effect indifferent whether such service is performed or not. O&M costs associated with directly assigned facilities and replacements should similarly be charged directly to the customer requiring these particular facilities.

~~2. Metering and meter reading services.~~

Comments: Appropriate metering, communications systems and meter reading services are required for determining the amount of power and energy that Affected Utilities wheel to end use customers from third party suppliers as well as determining the total amount of power that the customer may have used from other suppliers including the Affected Utilities. Otherwise, ancillary services will need to be provided by the host control area utility.

If the customer subscribes for full requirements service from a control area utility, this service should be bundled in a Customer Services Charge. The incumbent utility should retain all metering responsibilities. Advantages include: economies of scale, non-discriminatory practices, efficient dispute resolution, clear point of delivery and legal responsibility.

With regard to transmission or distribution wheeling services that a host control area utility is required to perform, if such service utilizes the utility's bulk transmission system, then the utility's FERC open access tariff will prevail. Given that metering requirements as well as other communication equipment requirements are generally the same whether the customer requests transmission or both transmission and distribution wheeling services, the control area utility's FERC transmission tariff should address responsibility for metering and communications equipment

Lastly, it must be noted that presently retail customer demand loads are generally measured over an integrated 15 minute period whereas wholesale customer loads (both requirements and wheeling) are determined using a 1 hour period. These are not consistent and one cannot simply substitute the retail integration period for that used for a wholesale customer taking transmission. Since the FERC tariff would prevail for most wheeling applications because the transmission system must also be utilized, Affected Utilities may be required to convert existing metering as well as rate redesign to conform to a one hour integration.

3. Open access transmission service (as approved by the Federal Energy Regulatory Commission, if applicable).

Comments: Retail wheeling customers requiring utilization of an Affected Utilities transmission system will be subject to the utility's FERC transmission tariff. It would therefore be imperative that all inconsistencies that preclude implementation of wheeling services, such as these addressed herein, be resolved prior to commencement of any retail wheeling programs.

4. Ancillary services as defined by the Federal Energy Regulatory Commission in Order 888 (III FERC Stats. & Regs. f 31,036, 1996).

Comments: In general, the ancillary services addressed in an Affected Utility's FERC transmission tariff are germane to retail wheeling and are applicable. However, as presently structured pragmatically they may not be applied to loads exhibiting retail load characteristics. For example, scheduling under APS and FERC transmission tariffs must be done in 1MW increments and energy imbalances similarly are accounted for in no less than 1MW increments.

Additionally, many of the ancillary services would require installation of relatively expensive telemetering equipment (RTUs, etc.) as well as software and communications requirements so that APS' Energy Management System can track such loads and have the system react in a manner consistent with those services for which the customer subscribes to versus acquiring from another entity.

It is undisputed that retail customers require ancillary services whether they be supplied by the Affected Utility or some other entity (if technically feasible). However, each individual application may be unique given the menu of ancillary service choices and the potential providers of such services. As in FERC's tariff, the customer would be responsible for the costs of such equipment and maintaining such equipment in good working order.

5. Information services such as provision of customer information to other suppliers.

Comments: Information about individual customer load and data may well be considered confidential by the customer even though it is in the utility's possession. Utilities traditionally recognize the privacy of their customers. They should not be made to disclose customer data unless the customer explicitly directs the utility to do so.

6. Other ancillary services necessary for safe and reliable system operation.

Comments: Although FERC's open access tariff does not require a utility to provide losses services as an ancillary service, one would expect that retail applications would certainly require such a service.

Additionally, losses for power and energy transmitted over the distribution system are higher than those incurred in wheeling over the bulk transmission system. These are also additive to transmission losses.

One would also expect that retail customers would require and demand a very high degree of reliability. In order to insure that the control area utility is equitably compensated for providing such reliability and not be "leaned on" without compensation, a customer who is taking energy service from another supplier would be required to subscribe for standby power from APS (unless dynamic signaling capability existed).

7. Customer services: A charge to recover the costs of metering, billing, collection, customer administration and services.

8. System Benefits.

Comments: As described above, we believe these services should be separately unbundled.

D. To manage its risks, an Affected Utility ***and generation supplier*** may employ reasonable credit checks, deposit requirements, and advance payment requirements for Unbundled Services ***and Generation Services.***

E. The Affected Utilities must provide transmission and ancillary services according to the following guidelines:

1. Services must be provided consistent with applicable tariffs filed with the Federal Energy Regulatory Commission.

Comments: Although this could be mandated for transmission and related ancillary services, there would be implementation problems as discussed above. FERC's tariffs do not generally address distribution wheeling service nor is FERC's accepted practices for ratemaking treatment of such facilities viable for large scale programs having large numbers of customers utilizing distribution facilities. See also comments above.

Lastly, the proposed rulemaking seems to assume that all Affected Utilities have "applicable tariffs filed with the Federal Energy Regulatory Commission." Such is not the case. None of the Co-ops, nor Ajo Improvement District, for example, are required to have such tariffs on file. In fact, APS is not sure that most of these entities even have transmission facilities. Thus, prices for unbundled ancillary services may not be available in their case.

2. Affected Utilities must accept power and energy delivered to their transmission systems by others and offer wheeling services comparable to services they provide to themselves.

Comments: This requirement cannot be legally imposed by the ACC on APS, because the Federal Power Act has preempted the states in this area. See comments to R14-2-xxx10. Also, as mentioned above, not all Affected Utilities even have transmission systems.

F. Upon authorization by the customer, ***a properly certified electric company*** shall release in a timely and useful manner that customer's load and usage data to a certificated supplier of services authorized by this Article.

1. The supplier of services shall provide the a properly certified electric company with a complete and accurate account number for the customer for which data is requested.

2. The properly certified electric company will be required to supply the monthly metered demand and total energy information as may reside in the Affected Company's billing information system.

3. The properly certified electric company shall provide such data for the current customer of record for the most recent twelve (12) billing months.

4. The properly certified electric company may provide such data in a form, either electronic or paper, mutually agreed to with the supplier of services.

G. Rates for Unbundled Services:

1. The Commission shall review and approve rates for services listed in Subsections R14-2-xxx6(C) and R14-2-xxx6(D), where it has jurisdiction, before such services can be offered.
2. Such rates shall reflect the costs of providing the services.

3. Such rates may be downwardly flexible if approved by the Commission.

H. Companies offering services under this Subsection R14-2-xxx6 shall provide adequate supporting documentation for their proposed rates. Where rates are approved by another jurisdiction, such as the Federal Energy Regulatory Commission, those rates shall be provided to this Commission.

* * * * * * *

R14-2-xxx7. Recovery of Stranded Investment of Affected Utilities

Comments: In the first part of its comments, APS has already demonstrated why full recovery of stranded investment is legally required to avoid an unconstitutional "taking" or confiscation of the Company's property and to compensate it for the Commission's impairment of APS' unambiguous contract with the State to be the exclusive provider of electricity within its service territory. For these reasons, APS objects to this provision of the Draft Rules which make recovery of stranded investment merely a matter of discretion to be decided by the Commission after the introduction of competition based on a laundry list of factors which are irrelevant to the Company's legal right to stranded cost recovery.

However, in addition to this legal reason and to the equity arguments favoring full recovery of stranded investment reflected in the President's Economic Report cited earlier, there are at least two additional reasons - economic efficiency and protection of customer interests - why full stranded investment recovery is appropriate. Recovery of stranded investment is required if increased competition in the electric industry is to result in increased economic efficiency in the production and sale of electric power (one of Staff's goals). As Dr. William Baumol observed in his recent book, Transmission Pricing and Stranded Cost in the Electric Power Industry, (AEI 199):

> ***At least two major types of inefficiency can result from a failure to adopt a defensible policy dealing with stranded cost: they can divert business to less efficient suppliers, whose higher operating costs are offset by freedom from any obligations imposed on the incumbent utility, and they can serve as a disincentive for future investment in the utility and condemn efficient suppliers to obsolescence and inadequate capacity. (Page 99).***

Competition can improve economic efficiency if the competition is based on the relative marginal costs of the competitors. However, if instead of rewarding the marginally efficient power producer and penalizing the marginally inefficient producer, competition is based on how successfully one group of customers can "game" the regulatory process to the detriment of other customer groups, there is no reason to expect improvements in overall economic efficiency. Quite the contrary - such a system might obscure the very real transactional costs of playing this game of musical power providers, thus leading to economically inefficient consumer choices.

Moreover, appropriate recovery of stranded investment is also in the customer's long-term best interest:

> ***If price reductions are imposed in a manner that prevents the firm from covering its costs - including, in particular, its cost of capital - the victory of consumers is entirely***

Pyrrhic. Their short-run gains will be more than offset by the future deterioration in service, for there is no way that the regulator or the courts can force investors to fund an uncompensatory enterprise. The market mechanism dooms such a firm to deterioration and ultimate extinction, as funding is denied it for maintenance, replacement, modernization and expansion of capacity, if expansion is required by growing demand. (Baumol, op cit. at 106).

For these reasons, APS asks the Commission to join the FERC and other state commissions by revising the stranded investment provisions to specifically provide for full recovery of properly defined and unmitigated stranded investment and to leave the quantification of such costs and the determination of the appropriate recovery mechanism to subsequent proceedings which can consider the specific circumstances of each utility.

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R14-2-xxx8. System Benefits Charges

A. By the date indicated in Subsection R14-2-xxx2, each Affected Utility shall file for Commission review rates or related mechanisms to recover the costs of System Benefits from all consumers located in the Affected Utility's service area who participate in the competitive market. ***In addition, the utility may file for a change in the System Benefits Charges at any time.***

B. Each Affected Utility shall provide adequate supporting documentation for its proposed rates for System Benefits.

C. An Affected Utility shall recover the costs of System Benefits only upon approval by the Commission of the recovery charge and mechanism.

Comments: The Draft Rule is not clear as to how the System Benefits Charges would be applied to consumers. If applied as a distribution surcharge within each Affected Utility's certificated area, then for those customers who take energy above distribution voltage, a means would have to be determined to collect the system benefits charges from them or other customers would have to bear the entire cost. For instance, for these customers the ACC could request that FERC determine that a portion of every transaction should remain under state jurisdiction. Alternatively, an Affected Utility and the Commission could request that FERC allow the charge to be imposed on their FERC transmission tariffs.

* * * * * * *

R14-2-xxx9. Solar Portfolio Standard

A. Starting on January 1, 1999, any company selling electricity under the provisions of this Article must derive at least 1 percent of the total retail energy sold competitively from New solar resources, whether that solar energy is purchased or generated by the seller. Solar resources include photovoltaic resources and solar thermal resources that generate electricity. New solar resources are those installed on or after January 1, 1997.

B. Starting on January 1, 2002, any company selling electricity under the provisions of this Article must derive at least 2 percent of the total retail energy sold competitively from new solar resources, whether that solar energy is purchased or generated by the seller. Solar resources include photovoltaic resources and solar thermal resources that generate

electricity. New solar resources are those installed on or after January 1, 1997.

C. Any company certificated under the provisions of this Article shall be able to credit two times the electric energy generated before January 1, 1999 using photovoltaics or solar thermal resources installed on or after January 1, 1997 in Arizona to the electric energy requirements of Subsections R14-2-xxx9(A) or R14-2-xxx9(B).

D. Companies selling electricity under the provisions of this Article shall provide reports on sales and solar power as required in this Article, and the Commission may conduct necessary monitoring to ensure the accuracy of these data.

E. If a company selling electricity under the provisions of this Article fails to meet the requirement in Subsection R14-2-xxx9(A) or Subsection R14-2-xxx9(B) in any year, the Commission may impose a penalty on that company up to $0.30 per kWh for deficiencies in the provision of solar energy. In addition, if the provision of solar energy is consistently deficient the Commission may void a company's contracts negotiated under this Article.

***Comments**: APS believes the Commission has no authority to void contracts lawfully entered into, as it would discourage the sort of long-term agreements necessary to finance new system capacity. Additionally, APS believes that the Commission cannot lawfully dictate the investment portfolio decisions of PSC's, let alone require that generation portfolios reflect specific technologies.*

~~F. The solar portfolio standard described in this Subsection is in addition to renewable resource goals for Affected Utilities established in Decision No. 58643.~~

***Comments**: APS continues to stress its belief that in a competitive energy marketplace market forces themselves must decide whether or not renewable (solar) should be a significant part of Arizona's energy production portfolio. The mandatory solar set asides as required under Rule R14-2-xxx9A and R14-2-xxx9B are an expensive proposition. APS estimates, based on its current demand forecast and existing solar cost levels, it would have to install over 200MWs of solar photovoltaic and/or solar thermal electric plants at an estimated investment cost of upwards of a billion dollars by the year 2003 to comply with these rules. We estimate this is nearly 10 times the investment that would be required to build combustion turbines with the same capacity. Furthermore, use of up to four (4) square miles or approximately 2400 acres land would be required to build the needed facilities.*

The proposed rule could deter competition. Competitors' market shares will change from year to year if not month to month making it difficult to project and obtain the required solar portfolio. some competitors (especially smaller ones) may choose to avoid the market and the potential penalties rather than be strapped with the difficulties of projecting market share and obtaining what may be an uneconomic resource. For other potential competitors (especially the larger ones) who decided to enter the market, it may be easier to pay the penalty in the first year or two than it will be to keep current on their solar portfolio in a changing market place. There would be a large amount of risk associated with the first solar resource in the market, which may also be the first to be abandoned when the newer more cost effective technology is available. Additionally, the rule may serve to discourage off-grid applications, by effectively forcing only central station installations in order to meet the large MW requirement. Under these various scenarios, the goal of the proposed rule, to create an Arizona solar market, would not be met.

Finally, the Draft Rule has no termination date for the solar portfolio. At some date renewables need to stand alone and be competitive without any government program.

As stated previously by APS, renewable sources of energy can be encouraged during the transition to a competitive market by promoting those applications where cost effectiveness can be achieved and/or have a reasonable expectation of being achieved. Specifically, renewables can be encouraged and the development of a viable renewables market can be assisted by continuing to support applications such as off-grid and multi-customer installations and providing an option for all grid-connected customers to access renewably generated energy. These are non-traditional applications for both utilities and customers alike. It is only through continued support of such applications during the period of transition that the market will develop as the expectations of customers, the experience of utilities and capabilities of manufacturers mature. APS believes the action plans currently in place would foster these developments.

If a solar program is created, we propose that the program properly support development of the solar industry in Arizona. The program must ensure the competitiveness of the resources constructed. The program must stand alone from the competitive docket process. Program costs, above the market, must be transparent to the consumer and neither incumbent utilities nor the energy sellers coming into the market should be straddled with uneconomic resources. Finally, any such program should exist only during the transition to a fully open market, at which time the market and new solar technology should combine to allow any subsequent new solar resources to compete without government program support.

APS believes the program structurally outlined below meets the above criteria:

> *The Corporation Commission sets a statewide goal for the installation and operation of solar generation. We propose a goal of 25MW statewide by December 31, 2000, with interim and subsequent goals, possibly 50 MW by December 31, 2004. These statewide goals would include any existing goals for existing utilities.*
>
> *A fixed fee will be collected on all kWh delivered to customers in Arizona starting June 1997. The money collected is placed in interest bearing financial accounts, and beginning in 1998, the money will be used to "buy-down" the uneconomic portion of the cost of newly installed solar in Arizona. This would be the only authorized use of the available money. The "buy-down" of the uneconomic portion of the construction costs will insure that the capacity can be sold competitively and limits the amount of money that needs to be collected by the fee.*
>
> *The money would be disbursed on a competitive-bid basis, in order to encourage the development of a competitive solar industry in the State. The competitive bid process will award grants to companies that commit to install and operate for a minimum term, new solar capacity in Arizona, for energy sale on a free-market basis. The competition for the grant should be based on who offers the maximum "MW per dollar" rather than a minimum "dollars for MW". The actual amounts installed will depend on the competitiveness of the bids received. The grants will be paid in thirds (at the time of grant, at substantial completion and after successful operations for 1 year) to attract only qualified bidders to force the bidders to put their own capital at risk, thereby making the process more*

competitive. Additional bidder qualifications will be needed including a commitment to the plant operation to avoid the "build and walk away" problems of the tax credit era.

Fee termination and the last grant disbursement should be arranged so that all construction under the program would be complete prior to the date the market is fully open to competition.

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R14-2-x10. Pooling of Generation and Centralized Dispatch of Generation or Transmission

A. The Commission shall conduct an inquiry into pooling and dispatch arrangements for transmission and generation of electricity.

B. The Commission may establish a pool for generation or centralized dispatch of generation or transmission by an independent system operator or by other means.

C. The Commission may work with other entities to establish pooling or centralized dispatch of generation or transmission.

Comments: This Section purports to recognize the Commission's authority to "establish a pool for generation or centralized dispatch of generation or transmission by an independent system operator or by other means." Interestingly, this purported authority does not appear to be restricted to Affected Utilities.

Section 201.(a) of the Federal Power Act[3] gives the Federal Energy Regulatory Commission (FERC) jurisdiction over "the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce." Under the doctrine of Federal supremacy, this means FERC has exclusive authority to regulate the transmission of electric energy in interstate commerce and the sale of such energy at wholesale.[4] Any attempt by the ACC to "establish a pool for generation or centralized dispatch of generation or transmission by an independent system operator" would constitute a direct challenge to FERC's jurisdictional authority and would probably fail. A generation pool cannot be formed without impinging on FERC's jurisdiction over wholesale sales, and an independent system operator (ISO) of transmission cannot be created without affecting the "transmission of electric energy in interstate commerce."

In California, these jurisdictional problems were overcome through an agreement between the California Public Utilities Commission (CPUC) and the State's three major electric utilities. Once the parties reached agreement in principle, the three utilities filed an application with FERC for approval of their pooling and ISO concepts. The CPUC intervened in the proceeding as a party and has made known its disagreement with certain details of the utilities' filing.

Accordingly, while the ACC may support the creation of a pool and ISO among Affected Utilities, it may not "establish" them through its orders. *Jurisdictional concerns aside, consideration of the issues of pooling and centralized dispatch are intertwined with the larger issue of preserving system reliability. APS believes a through examination of this large reliability issue needs to begin immediately.*

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[3] 16 USC §§791a-825r.

[4] *See Mississippi Power & Light Co., v. Mississippi et al*, 487 U.S. 354, 108 S.Ct. 2428 (1988).

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R14-2-xxx11. In-State Reciprocity

The service territories of Arizona electric utilities which are not Affected Utilities shall not be open to competition under the provisions of this Article, nor shall Arizona electric utilities which are not Affected Utilities be able to compete for sales in the service territories of the Affected Utilities. However, an Arizona electric utility (***or an affiliate of an Arizona Electric Utility***) which is not an Affected Utility may voluntarily participate under the provisions of this Article if it makes its service territory available for competing sellers, if it agrees to all of the requirements of this Article, and if it obtains an appropriate Certificate of Convenience and Necessity.

Comments: See comments on R14-2-xxx3 re application to Non-PSCs and to out of state suppliers and concerning the ability of Affected Utilities to compete with other Affected Utilities.

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R14-2-xxx12. Rates

A. Market based rates for competitively provided services ***as defined in Subsection R14-2-xxx5*** shall be deemed to be just and reasonable.

B. Each company selling services under this Article shall have on file with the Commission tariffs describing such services and maximum rates for those services, but the services may not be provided until the Commission has approved the tariffs.

C. For competitive services provided under standard contracts (that is, non-customized rates, terms, and conditions), a company governed by this Article shall file in a timely manner with the Director of the Utilities Division current price lists. terms and conditions consistent with approved tariffs.

D. Competitively negotiated contracts customized to individual customers which comply with approved tariffs do not require further Commission approval. However, all such contracts must be filed with the Director of the Utilities Division ***pursuant to R14-2-xxx15(C)*** at least 30 days prior to becoming effective; if a contract does not comply with the provisions of this Article it shall not become effective without a Commission order.

E. An Affected Utility or company holding a Certificate pursuant to this Article may price its competitive services, as defined in Subsection R14-2-xxx5, at or below the maximum rates specified in its filed tariff, provided that the price is not less than the marginal cost of providing the service.

F. Requests for changes in maximum rates or changes in terms and conditions of previously approved tariffs may be filed. Such changes become effective only upon Commission approval .

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R14-2-xxx13. Service Quality, Consumer Protection, Safety, and Billing Requirements

Comments: Rather than create separate quality, consumer protection, safety and billing rules for new competitive entrants or for new competitive services, existing Commission regulations (where

applicable) should be uniformly applied. Indeed, the Staff should consider folding any new regulation into the existing Article 2 regulations on electric PSCs.

A. All customer bill complaints concerning services rendered under this Article shall be governed by the provisions of Subsections R14-2-212(B) and R14-2-212(C).

Comments: Need clarification that bill complaints will be between, and resolved by, the supplier of the service and the customer, regardless of who is providing the billing.

Need to define or eliminate "utility" as used in the sections mentioned.

B.1 would read: "Any customer who disputes a portion of a bill rendered for service shall pay the undisputed portion of the bill and notify the service supplier's designated representative in writing that such unpaid amount is in dispute prior to the delinquent date of the bill."

B.2 would read: "Upon written receipt of the customer notice of the dispute, the service supplier shall:

- ***a. Notify the customer within five working days of the receipt of a written dispute notice.***
- ***b. Initiate a prompt investigation as to the source of the dispute.***
- ***c. Withhold disconnection of service until the investigation is completed and the customer is informed of the results. Upon request of the customer the service supplier shall report the results of the investigation in writing.***
- ***d. Inform the customer of his right of appeal to the Commission."***

B.3 would read: "Once the customer has received the results of the service suppliers investigation, the customer shall submit payment within five working days to the billing company for any disputed amounts. Failure to make full payment shall be grounds for termination of service."

In R14-2-212(c), the word "service supplier" should replace utility.

B. All customer service complaints concerning services rendered under this Article shall be governed by the provisions of Subsections R14-2-212 (A) and R14-2-212(C).

C. Establishment of competitive service**s** to consumers ~~whose estimated demand is less than 1,000 kilowatts~~ shall be governed by the provisions of Subsections R14-2-203(A) ~~and R14-2-203 (B)~~ ***through R14-2-203 (E) and R14-2-204 (A) and (B).***

Comments: The rule should apply regardless of customer size.

D. No consumer shall be deemed to have changed suppliers of any service authorized in this Article (including changes from supply by the Affected Utility ***or a new supplier*** to another supplier) without written authorization by the consumer for service from the new supplier. If a consumer is switched to a different ("new") supplier without such written authorization, the new supplier shall cause service by the previous supplier to be resumed and the new supplier shall bear all costs associated with switching the consumer back to the previous supplier.

Comments: This could be interpreted that if a customer is moving from one address in another suppliers certificated area, the existing supplier can continue to bill for services until the customer

provides written notification requesting service from a new supplier. This will create administrative confusion as well as customer frustration.

The intent of this section needs to be clarified to indicate it applies to consumers staying at an existing premise. Additionally, issues regarding who can authorize the switch (only the customer of record, roommates, second tenants, etc.), the ability for previous supplier to collect from the new supplier, what is meant by "all costs" (does this include billed electric revenue that may have occurred).

E. Each company providing service governed ***under*** ~~by~~ this Article shall be responsible for maintaining in safe operating condition all equipment owned by and under the control of that company that is used to provide electric service to its customers ***and shall be governed by Subsection R14-2-208.***

F. Responsibilities of suppliers of ***electric*** distribution service and of customers receiving distribution service are governed by Subsection R14-2-208.

G. Each company providing service governed by this Article shall be responsible for meeting applicable reliability standards and shall work cooperatively with other companies with whom it has interconnections, directly or indirectly, to ensure safe, reliable electric service. Construction standards and safety for each company providing service under this Article are governed by Subsection R14-2-208(F).

Comments: The Company agrees with the need to set Construction Standards and Safety but would appreciate the clarification of who (1)Sets the Applicable Reliability Standards (2) Liability of the Provider for disruptions in service caused by others (3) What force majeure protection given to provider (4) How will ACC impose Construction Standards and Safety over "Foreign Utilities.

H. Termination of service

1. Termination of service prior to the termination date specified in the contract with the consumer ~~is~~ ***shall, in addition to any requirements set forth in the contract, comply with the provisions of A.A.C.*** ~~governed by Subsection~~ R14-2-211.

Comments: Consumers should receive benefits of contractual protections against early termination in addition to those granted by rule.

2. ~~In addition to the above requirement, a~~ ***A***ny provider of service to consumers shall ***also*** provide at least ~~14~~ ***60*** days notice to all of its affected consumers if it is no longer obtaining generation, transmission, distribution, or ancillary services necessitating that the consumer obtain service from another supplier of generation, transmission, distribution, or ancillary services.

Comments: APS would suggest that the notification period be expanded to 60 days even if termination is pursuant to the expiration of a contract in order to give consumers more time to obtain a new supplier. In addition, if Affected Utilities retain an obligation to serve returning customers, the 60 days would provide Affected Utilities with sufficient time to ensure they have the required resources.

I. All companies providing service under this Article shall provide accident reports as provided in Subsection R14-2-101.

J. A company providing firm electric service governed by this Article shall make reasonable efforts to reestablish service within the shortest possible time when service interruptions occur and shall work cooperatively with other companies to ensure timely restoration of service where facilities are not under the control of the company ***and shall be governed by R14-2-209 and R14-2-210***.

Comments: This is covered in Subsection R14-2-208 and included in Paragraph (f) above. If not deleted, this Paragraph needs clarification of (1) What is the shortest possible time (2) what is firm service and (3) what do you consider timely.

K. Each company providing service governed by this Article shall bill monthly for services rendered ***shall be governed by R14-2-209 and R14-2-210***. ~~The following minimum information must be provided on all customer bills, whether the bill is rendered by the company or by another party on behalf of the company:~~

~~1. The amount of each service provided.~~

~~2. The monthly charges for each service provided.~~

~~3. The company's toll free telephone numbers for billing, service, and safety inquiries and the telephone number of the Consumer Services Section of the Arizona Corporation Commission Utilities Division.~~

~~4. The amount or percentage rate of any privilege, sales, use, or other taxes that are passed on to the customer as part of the charge for the service provided.~~

~~5. The date on which the bill becomes delinquent.~~

Comments: One item to consider is the expense of the customer calling toll free locally. Service suppliers should have the option of printing a local number for local customers and toll free numbers for customers where the call would be long distance.

L. A company providing service governed by this Article may include in its tariffs a fee for each instance where a customer tenders payment with an insufficient funds check ***as governed by R14-2-210(F)***.

Comments: Clarification will be needed as to whether more than one service supplier can impose the insufficient funds charge ("ISF"). For example, if a customer is purchasing energy from TEP and all other services from APS, and APS is providing the billing and the customer remits an ISF check, can TEP and APS both impose their ISF fee?

M. A company providing service governed by this Article may include in its tariffs a late payment penalty which may be applied to delinquent bills. The amount of the late payment penalty shall be stated on the customer's bill.

Comments: Same comments as section L above. Also, how are the receipts from a partial payment dispersed if more than one supplier?

N. Working group on system reliability and safety

1. The Commission shall establish, by separate order a working group to monitor and review system reliability and safety.
   a. The working group may establish technical advisory panels to assist it.
   b. The working group shall commence activities by the date indicated in Subsection R14-2-xxx2.
   c. Members of the working group shall include representatives of Staff, consumers, utilities, and other suppliers.
   d. The working group shall be chaired by the Director of the Utilities Division of the Commission or by his or her designee.
2. All companies governed by this Article shall cooperate and participate in any investigation conducted by the working group. including provision of data reasonably related to system reliability or safety.
3. The working group shall report to the Commission on system reliability and safety annually, and shall make recommendations to the Commission regarding improvements to reliability or safety, with the first report due no later than ~~March 31, 1998~~ ***mid 1997.***

Comments: APS would support the idea of establishing an ad hoc reliability working group as soon as practicable for purposes of reviewing the current electric system design practices of generation and interconnected transmission systems. Upon gaining this knowledge, the working group should develop reliability standards and protocols for the continued protection of the reliability of the regional interconnected high voltage transmission and state's electrical distribution systems, consistent with WSCC and NERC guidelines. APS believes once these standards are protocols and established, they should become enforceable on all electric services suppliers operating in the state of Arizona.

APS also suggests in addition to enforcing the new reliability rules, the existing Integrated Resource Planning (IRP) rules should also be amended to include all suppliers of generation and energy services in the state. Such entities should provide the Commission with the same information relative to resource plans as are or will be required of Affected Utilities in the future. Such information should include plans for long-term supply procurement of generation and transmission resources and adhere to presently established reliability standards.

The issues of reliability are extremely complex and not easily understood. For this reason technical forums currently exist where these complex issues can not only be discussed and evaluated, but where guidelines which ensure the integrity of the system for all can be and are established. Such are the roles of the WSCC and NERC, the promulgated guidelines of which are subscribed to by all affected utilities

System reliability comes about from the closely coordinated planning and operations of the interconnected system based upon established procedures. The standards of reliability which APS adheres to today are based upon many years of coordinated and careful planning, designing and constructing of generation, transmission, and distribution facilities to serve our customers electric demand requirements. These planning and operating activities call for the performance of complex engineering which include highly technical regional system stability analyses, power flow analyses, voltage control analyses , and the identification of system operating limits, the impacts of which go well beyond State boundaries. The interconnected distribution and high voltage transmission lines

with other utilities are closely coordinated and follow engineering and policy rules. Historically, electric utilities have placed sufficient generation resources to insure adequate reserve margins to meet customers' peak load demand. Fuel diversity planning and its significant benefits to the electric system is also a part of the engineering analysis. Regional and subregional engineering and policy committees (working groups) already exist to represent APS and the State's other electric utilities. Many of the State's generation and transmission assets are jointly-owned by in-state and out-state utilities.

O. Affected Utilities and other parties offering service under the provisions of this Article shall comply with applicable reliability standards and practices established by the Western Systems Coordinating Council and the North American Electric Reliability Council or successor organizations.

P. Affected Utilities and other certificated companies shall provide notification and informational materials to consumers about competition and consumer choices as ordered by the Commission.

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R14-2-xxx14. Reporting Requirements

A. Reports covering the following items shall be submitted to the Director of the Utilities Division by Affected Utilities and all companies granted a Certificate of Convenience and Necessity pursuant to this Article. These reports shall include the following information pertaining to competitive service offerings, Buy-throughs, Unbundled Services, and Standard Offer services provided pursuant to the FERC regulated transmission tariffs:

1. Type of services offered.

Comments: APS seeks clarification of the meaning of competitive service offerings. One needs to recognize that some of the service offerings to retail customers fall under the jurisdiction of the FERC and as such should not be subject to ACC reporting requirements. These service offerings include such services as regulation and frequency response, energy imbalance, operating and spinning reserve, and standby power services.

2. kW and kWh of sales, disaggregated by customer class (e . g ., residential, commercial, industrial).

Comments: The reporting of kW and kWh of sales disaggregated by class should be expanded to include sales to marketers and/or aggregators who purchase directly from the local utility company or other third party supplier. The sales to end users at the residential, commercial and industrial level should be reported by the marketers and/or aggregators buying from the local utility. Such entities as noted earlier should be required to have a Certificate of Convenience and Necessity and should be subject to the same reporting requirements as affected utilities.

3. Solar energy sales (kWh) and sources.

Comments: APS suggests that at least for off-grid applications, solar sales only be reported in terms of installed demand. To require kWh metering in such applications would simply add to the cost of

the installation by requiring a kWh meter which would serve no useful purpose outside of complying with a reporting requirement.

4. Revenues from sales by customer class (e.g., residential. commercial, industrial).
5. ~~Number of customers disaggregated by size of contract load (0-99 kW, 100 kW-499 kW, 500 kW-999 kW, 1 MW - 9.999 MW, 10 MW - 49.999 MW, and 50 MW and above).~~
6. Number of customers disaggregated by class (e . g ., aggregators, residential, commercial, industrial).
7. ~~kWh sales and revenues disaggregated by term of the contract (less than one year, one to four years, longer than four years). and by type of service (for example, firm interruptible, other).~~

Comments: With the potentially high volume of individual contracts which will characterize a world of open access, APS believes it would be overly burdensome to report kWh sales and revenues for each individual contract by term and type of contract provided for in sections 14.A.5 and 14.A.7 above. APS proposes such sales be reported on an aggregated, class basis consistent with the provisions of sections 14.2.A.2 and 14.2.A.6.

8. Amount of and revenues from each service provided under Subsection R14-2-xxx5, and, if applicable, Subsection R14-2-xxx6.
9. Value of all Arizona specific assets and accumulated depreciation.
10. Other data requested by Staff or the Commission.

B. Reporting Schedule:

1 For the period through December 31, 2003, semi-annual reports shall be due on April 1 (covering the previous period of July through December) and October 1 (covering the previous period of January through June). The first such report shall cover the period January 1 through June 30, 1998.

2. For the period after December 31, 2003, annual reports shall be due on April 1 (covering the previous period of January through December). The first such report shall cover the period January 1 through December 31, 2004.

C. The information listed above ~~may be~~ ***is*** provided on a confidential basis. ~~if reasonable to do so.~~ However, Staff or the Commission may issue reports with aggregate statistics based on confidential information that do not disclose data pertaining to a particular seller or purchases by a particular buyer.

Comments: The issue of confidentiality is one which will take on greater and greater importance as competition is introduced into the electric power industry. APS recommends that sensitive and proprietary information core to a utility's competitive advantages not be filed. Such filings are anticompetitive and at odds with the intention of the rules if the ACC will not guaranty confidential treatment of the information filed. Also, customers may object to information being filed which discloses or can be interpreted to disclose sensitive information about their operating costs, including the cost they pay for electricity. Therefore, if required to be filed it is incumbent upon the ACC to establish guaranteed processes to avoid intentional, optional or unintended disclosure, coupled with penalties for failure to comply with confidentiality requirements. The ACC must

assure that this information will not be available for public review or review by competitors, nor may it be retrieved by state requests.

The provisions of subparagraph C. do not go far enough. Optional confidentiality is insufficient given the materially sensitive nature of the information. The introduction of competition into the marketplace makes this mandatory. The standards and assurances set in subparagraph C are too loose and relaxed.

D. Any company governed by this Article which fails to file the above data in a timely manner may be subject to penalty imposed by the Commission or may have its Certificate rescinded by the Commission.

Comments: APS would like to reinforce Staff's position that any company failing to comply with any reporting requirements (and any other requirements imposed on affected utilities) should be subject to penalties up to and including revocation of its CC&N.

E. Any company holding a Certificate pursuant to this Article shall report to the Director of the Utilities Division the discontinuation of any competitive tariff as soon as practicable after the decision to discontinue offering service is made.

Comments: APS agrees that all companies holding a Certificate which should include marketers and aggregators, should notify the Commission of any discontinuance of competitive tariffs as soon as possible. Reporting requirements should be flexible enough to accommodate the frequency with which new tariffs may be developed and old ones canceled, but also allow sufficient time for alternative providers to respond when such tariff cancellations reflect a cancellation of service. This is especially important for the local utility who may be designated the provider of last resort. In such cases the term " as soon as possible" will need to be defined.

F. In addition to the above reporting requirements, companies governed by this Article shall participate in Commission workshops or other forums whose purpose is to evaluate competition or assess market issues.

Comments: In order for such workshops to be of any value it is imperative that they be mandatory for all market players, especially all new market entrants such as aggregators, brokers and marketers. Without their participation, discussions of market issues and evaluations of competition will be inadequate and meaningless.

G. Reports filed under the provisions of this Subsection R14-2-xxx14 shall be submitted in written format and in electronic format. Companies shall coordinate with the Commission Staff on formats.

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R14-2-xxx15. Administrative Requirements

A. Each company governed by this Article shall file with the Director of the Utilities Division a written statement containing the name, business address, and telephone numbers of at least one officer, agent, or employee responsible for the general

management of its Arizona operations. This information shall be updated, in writing, within five days from the date of any change.

B. Any company certificated under this Article may propose additional ***electrical*** services at any time by filing a proposed tariff with the Commission describing the service, maximum rates, terms and conditions. The ***proposed new electrical*** service may not be provided until the Commission has approved the tariff. ***The Commission will act on filings for new electrical services within thirty (30) days.***

C. Contracts filed pursuant to this Article shall not be open to public inspection or made public ~~except on order of the Commission, or by the Commission or a Commissioner in the course of a hearing or proceeding~~ ***under any conditions.***

Comments: ACC should not reserve authority to disclose. Cf. Staggers Rail Act of 1980, where Congress required the filing of rail transportation contracts with the Interstate Commerce Commission, but did not allow for their disclosure to the public. The suggestion here is potentially dangerous and may cause substantial unfair or anticompetitive effects.

D. Each company governed by this Article shall keep general and subsidiary accounting books and records reflecting the cost of its Arizona properties assets and liabilities, operating ***revenues,*** income and expenses, and all other accounting and statistical data which reflect complete, authentic, and accurate information regarding its properties and operations. These records shall be organized and maintained in such ~~as~~ way as to provide an audit trail through all segments of the company's accounting system.

E. Each company governed by this Article shall maintain its books and records in accordance with Generally Accepted Accounting Principles as promulgated by the Financial Accounting Standards Board and its successors, as amended***, with reconciliation to the reporting requirements of the FERC under 18 CFR Part 101 and 125 as adopted in R14-2-212G2.***

F. ~~All Companies~~ ***Each company*** governed by this Article shall ~~immediately~~ make available ***within 30 days,*** at the time and place the Commission may designate, any accounting and related records pertinent to the subject matter of this Article that the Commission may request.

G. ~~All Companies~~ ***Each company*** governed by this Article shall file with the Director of the Utilities Division a copy of all annual reports required by ***the State of Arizona,*** the Federal Energy Regulatory Commission or by the Securities and Exchange Commission.

H. The Commission may consider variations or exemptions from the terms or requirements of any of the rules in this Article upon the application of an affected party. The application must set forth the reasons why the public interest will be served by the variation or exemption from the Commission rules and regulations. Any variation or exemption granted shall require an order of the Commission. Where a conflict exists between these rules and an approved tariff or order of the Commission, the provisions of the approved tariff or order of the Commission shall apply.

I. The Commission may develop procedures for resolving disputes regarding implementation of retail electric competition.

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